

No. 83040-1

IN THE SUPREME COURT
OF THE STATE OF WASHINGTON

LEE H. ROUSSO,

Petitioner,

v.

STATE OF WASHINGTON,

Respondent.

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**BRIEF OF AMICI CURIAE
CHERYL AND JOHN BLAKE, ROB ESENE, AND JIM GAULEY
IN SUPPORT OF LEE H. ROUSSO**

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TABLE OF CONTENTS

TABLE OF AUTHORITIES.....	ii
STATEMENT OF INTEREST.....	1
ARGUMENT	1
I. Washington can more effectively regulate Internet poker than it can its in-state card rooms.	3
A. Washington can apply its licensing model to Internet poker websites.	3
B. Modern technologies render Washington’s regulatory regime stronger as applied to online card rooms and empower the State to deploy far more effective and pervasive controls.....	5
II. Several jurisdictions have successfully implemented robust regulatory regimes to govern Internet poker and others are considering doing so.....	7
A. Isle of Man (“IOM”).....	7
B. Italy.	11
C. France.....	12
D. The United Kingdom, Alderney and Gibraltar.	13
E. United States.	14
F. State Initiatives.....	16
III. The State has offered no support for its claim that it is powerless to regulate Internet poker.....	17
CONCLUSION.....	19

TABLE OF AUTHORITIES

Cases

<i>In re Globe Newspaper Co.</i> 729 F.2d 47 (1st Cir. 1984).....	1
--	---

Statutes

State:

RCW 9.46.070.....	4
RCW 9.46.071.....	4
RCW 9.46.130.....	4
RCW 9.46.140.....	4
RCW 9.46.160.....	4

France:

Texte Adopté no. 438, Apr. 6, 2010.....	13
---	----

Gibraltar:

Gambling Act, 2005.....	14
-------------------------	----

Isle of Man:

Criminal Justice (Money Laundering – Online Gambling) (No. 2) Code, 2008.....	10
Online Gambling Regulation Act, 2001.....	<i>passim</i>

United Kingdom:

Gambling Act, 2005.....	14
-------------------------	----

Regulatory Material

Federal:

Customer Identification Program for Banks, 31 C.F.R. § 103.121
(2009).....6, 10

Special Rules for Casinos, 31 C.F.R. § 103.64 (2009).....10

State:

WAC 230-06-010.....4

WAC 230-06-015.....4

WAC 230-06-035.....4

WAC 230-15-025.....4

Alderney:

eGambling Regulations, 2009.....14

Isle of Man:

Isle of Man Gambling Supervision Commission, *Guidance for On-line
Gambling* (Jan. 15, 2010).....*passim*

The Online Gambling (Systems Verification) (No. 2) Regulations,
2007.....8

United Kingdom:

Dep't for Culture, Media, and Sport, *Gambling Act 2005 "White-Listing"*
(Jan. 2007).....10–11

Gambling Commission, *Conditions and Codes of Practice 8*
(Dec. 2008).....14

Pending Legislation

Federal:

Bipartisan Tax Fairness and Simplification Act of (2010), S. 3018, 111th Cong. (2010).....14–15

Internet Gambling Regulation, Consumer Protection, and Enforcement Act, H.R. 2267, 111th Cong. (2009).....16

Internet Poker and Game of Skill Regulation, Consumer Protection and Enforcement Act of 2009, S. 1597, 111th Cong. (2009).....16

State:

Internet Poker Consumer Protection & Revenue Generation Act of 2010, H.B. 1441, 2010 Reg. Sess. (Fla. 2010).....16–17

S. 490, 214th Leg. (N.J. 2010).....17

Other Materials

Age Verification: State of the Art, Statement of the Market.....4

Bruce P. Keller, *The Game's the Same: Why Gambling in Cyberspace Violates Federal Law*, 108 Yale L.J. 1569 (1999).....18–19

Fin. Action Task Force, *United States of America: Report on Observance of Standards and Codes* (Sept. 2006).....10

Francois Peglau, GamblingCompliance Ltd., *Italy* (Mar. 5, 2010).....11–13

Int'l Monetary Fund Legal Dep't, *Isle of Man: Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism* (Sept. 2009).....10

Malcolm K. Sparrow, *Can Internet Gambling Be Effectively Regulated?: Managing the Risks* (Nov. 11, 2009).....passim

Pat Rodrigue, GamblingCompliance Ltd., <i>France</i> (Apr. 16, 2010).....	13
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STATEMENT OF INTEREST

Amici curiae Cheryl and John Blake, Rob Esene, and Jim Gauley are poker players who want to compete in poker games on the Internet, using gaming sites like PokerStars.com. While they may lawfully play poker in Washington's brick-and-mortar card rooms, which are licensed, regulated and taxed by the State, they face criminal prosecution and imprisonment for five years if they play the same games online.

ARGUMENT

The State has taken a position in this litigation at odds with both the current state of technology and of the law. Because its online poker prohibition undeniably protects its highly regulated in-state card rooms from competition, the State embraced as a litigation strategy the notion that Internet gaming is ungovernable. "None of the normal regulatory safeguards" that it applies to its in-state card rooms, the State asserts, "can be effectively enforced" online. Supplemental Br. of Resp't 11 (hereinafter "State Br."). Because the Commerce Clause does not oblige a State to do that which is impossible, the State argues that it need not treat evenhandedly its in-state poker industry and poker sites that operate beyond its borders.

The State offers "a comfortable doctrine, to which we can have but one objection: namely, that it is not true." *In re Globe Newspaper Co.*, 729 F.2d 47, 54 (1st Cir. 1984) (internal quotation omitted). Experts have

rigorously debunked the State's outdated "perception that online gambling—in contrast to gambling in bricks-and-mortar casinos—would be difficult, if not impossible, to regulate effectively." Malcolm K. Sparrow, *Can Internet Gambling Be Effectively Regulated?: Managing the Risks* 1 (Nov. 11, 2009) (hereinafter "Sparrow," attached as Ex. A). For example, Professor Sparrow, an expert in fraud controls, regulatory processes, and risk management at Harvard's Kennedy School of Government, recently concluded that: (i) "Online gambling could be regulated effectively;" (ii) "[a] well-structured regulatory regime should provide much better social and consumer protections than [prohibition];" and (iii) "even an imperfect legalization and regulatory regime for online gambling" would offer "much more protection" than flat prohibition. *Id.* at 2.

The State's fundamental premise is flawed. In fact, Washington could both apply its current regulations with greater success online and adopt *additional* controls made possible by Internet technology. *Id.* (explaining that "several of the risks" of gambling "become *more* amenable to control online"). Several jurisdictions—including the Isle of Man, Italy, France and the U.K.—have found success where Washington insists only futility can be found, and other jurisdictions—such as the U.S. government, Florida and New Jersey—are actively considering similar regulatory efforts.

The State has not addressed these actual regulations of online gaming, and has offered no evidence to support its assumption that regulation is impossible. Nevertheless, the State secured summary judgment in its favor—depriving plaintiff Rousso of even an opportunity to prove his claim. This Court should vacate the judgment below and remand the matter for further proceedings.

I. Washington can more effectively regulate Internet poker than it can its in-state card rooms.

A. Washington can apply its licensing model to Internet poker websites.

As the State seems to concede, the potential problems posed by unregulated Internet poker are, in large part, the same problems posed by gambling generally.¹ Washington has, of course, surmounted these problems as far as its in-state card rooms are concerned. Poker play is legal in those card rooms, subject to the State's comprehensive gambling laws. In the State's words, those laws "are based on a licensing model that requires all entities operating gambling businesses and, in many instances, their

¹ *E.g.*, State Br. 12 ("[I]nternet gambling, like other types of unregulated gambling activities, poses a significant risk to the health, welfare and morals of residents of the State of Washington."). Washington broadly relies upon "the social and economic problems that accompany gambling" that have been "long recognized" by "Washington's constitution, the Legislature, and its courts." *Id.* at 8. And it premises the State's "legitimate local public interest in restricting and regulating gambling through The Gambling Act" upon "the far-reaching social impacts and costs associated with gambling" in general. *Id.* at 10.

individual employees, to subject themselves to close state scrutiny and ongoing regulation.” *Id.* at 11.²

Washington could employ online the same regulatory strategy that has enabled it to overcome the perils of gambling in its in-state card rooms— Indeed, in other contexts the State seems to have had little problem doing exactly that. *See* Br. of Amicus Curiae The Poker Players Alliance 12–13 (describing regulation of electronic wagering on horse racing). Its criminal background checks—or more extensive checks—could be made a requirement of licensure for an online poker site. And the State could apply its strict accounting standards and demand the right to inspect records and to audit financials. Similarly, online poker sites could be required to verify players’ identities.³ And with the stroke of a pen, the State could limit hours of operation and prohibit gambling on credit.

² Specifically, the State requires licensees to submit to criminal background checks, RCW 9.46.070 & RCW 9.46.160; requires licensees to open their books for inspection “to ensure compliance with state laws designed to safeguard the public and prevent criminal infiltration,” RCW 9.46.130; requires “adhere[nce] to strict accounting standards and submi[ssion] to audits of . . . financial records and books to ensure proper payouts, tax payments, and to ferret out graft and corruption,” RCW 9.46.070, 9.46.130 & 9.46.140; prohibits gambling on credit, WAC 230-06-035; limits the hours licensees can operate, WAC 230-15-025; and prohibits certain persons from gambling, RCW 9.46.071, WAC 230-06-010 & WAC 230-06-015. *See* State Br. 2–3.

³ *E.g.*, Sparrow 16–22; Age Verification: State of the Art, Statement of the Market, <http://integrity.aristotle.com/content/view/312/194/> (2005 video demonstrating an age verification system that prevented underage access to Internet gaming).

B. Modern technologies render Washington's regulatory regime stronger as applied to online card rooms and empower the State to deploy far more effective and pervasive controls.

Washington could "ferret out graft and corruption" and "ensure proper payouts [and] tax payments" far more effectively online than it can in its in-state card rooms. "Comprehensive electronic records and the ability to track financial transactions and betting patterns provide more opportunities for analysis and audit, and hence improve the chances of discovering fraud or criminal activity." Sparrow 2. An Internet card room can "retain comprehensive data on all deposits, withdrawals, and betting transactions and . . . make these available to regulators for examination and analysis." Sparrow 42. Technology "for detecting anomalies and suspicious behavior may be operated easily and routinely on [these] digital databases" by "operators, regulators, or both." *Id.*

Given this "complete data," the task of policing accounting procedures, tax compliance and gaming controls is dramatically simplified. *Id.* Similarly, because "most patterns related to money laundering (such as light betting or matched bets placed by collaborators) would be easier to detect than they are in a physical environment (where complete transaction histories are available only in the form of video recordings)," the State could far more effectively detect illicit uses of gaming services—by site operators

and customers alike. *Id.* Finally, in light of this data, strict “know your customer” rules can be imposed on Internet poker venues—like those the U.S. imposes on financial institutions. Sparrow 37–42; *see* Customer Identification Programs for Banks, 31 C.F.R. § 103.121 (2009).

The fundamental point is simple: because online card rooms can be compelled to accumulate and make available vast stores of data—unlike their lawful, in-state counterparts—their operations can be more rigorously scrutinized and subjected to heightened and more nuanced control. But the implications are profound. One compelling example is Washington’s unique opportunity to combat problem gambling in online card rooms. Unlike Washington’s in-state card rooms, online poker sites can deploy “tools to mitigate problem gambling in a timely manner.” Sparrow 2. “In a well-regulated online environment,” these technologies would “help curb addictive or problematic gambling behaviors.” *Id.* at 12. Operators might, for example, be required to identify poker play patterns characteristic of problem gamblers and to “limit [such gamblers’] gambling volume, deposit rates, loss rates, [or] the size of each wager.” *Id.* Online poker players “could also access online clinical and self-help resources from links provided at the” card rooms. *Id.*

The State gets matters exactly backwards. Its power to combat the potential ills of gambling as they may be manifested in a poker card room is

greatly enhanced, not thwarted, if that card room exists online rather than within the State's borders.

II. Several jurisdictions have successfully implemented robust regulatory regimes to govern Internet poker and others are considering doing so.

To further illustrate the fallacy of the State's position, amici offer a non-exhaustive review of comprehensive regulatory regimes that are in existence (Isle of Man, Italy, France and the U.K.) or under consideration (U.S., Florida and New Jersey). For instance, PokerStars.com, a site that amici would patronize absent the State's prohibition on Internet poker, is licensed in the Isle of Man and in Italy.

A. Isle of Man ("IOM").

The IOM has been recognized as a world leader in the effective regulation of online gaming. For example, it is one of only four jurisdictions on the UK's "whitelist" of non-European Economic Area countries. See Dep't for Culture, Media, and Sport, *Gambling Act 2005 "White-Listing"* § 1.1 (Jan. 2007).⁴ The IOM began licensing and regulating Internet gaming in

⁴ Available at

<http://www.culture.gov.uk/images/publications/WhiteListingCriteria.pdf>. In being whitelisted, the IOM has "demonstrat[ed]" that "like the U.K.," it has "appropriate mechanisms in place to combat any criminality which may be linked to gambling. *Id.* § 3.7. As a result, U.K. residents may lawfully use IOM-licensed gaming websites to play cards.

2001, with passage of its Online Gambling Regulation Act (“OGRA”).⁵ To ensure its ability to regulate effectively, IOM requires that each licensee incorporates in the IOM, *id.* at § 4(1), locates its servers in the IOM for inspection, maintains gaming and trading accounts in a bank located in the IOM, and designates at least two corporate directors who reside in IOM—in addition to a resident “Designated Official” or “Operations Manager” who must answer to the Commission. Isle of Man Gambling Supervision Commission, *Guidance for On-line Gambling* § 1.2 (Jan. 15, 2010) (hereinafter, “Guidance”).⁶ Operators must also archive comprehensive data—data that both makes compliance possible and allows for regulatory supervision. Guidance § 3.5.17.⁷

OGRA is implemented by the IOM Gambling Supervision Commission, which is charged, broadly, with “[k]eep[ing] gambling crime free; [p]rotect[ing] the young and vulnerable; and . . . [e]nsur[ing] that the facilities offered by [IOM] licensees are fair and that players receive their

⁵ All IOM legislative materials are available at <http://www.gov.im/gambling/regulatory.xml> unless otherwise noted (all websites cited last accessed on Apr. 26, 2010).

⁶ Available at <http://www.gov.im/lib/docs/gambling/externalguidanceev3.doc>.

⁷ For example, operators must record, for each hand: the identity of each participant, the time the hand began, the balance in participants’ accounts at the outset and end of the hand, time-stamped records of the participants’ wagers, a time-stamped record of the hand’s results, the time the hand ends, the amount won or lost by each participant, and the currencies used by the participants. Guidance § 3.5.17; see The Online Gambling (Systems Verification) (No. 2) Regulations 2007 Sched. 1, § 10. Additionally, they must store information about large wins, large fund transfers, and “material fluctuations in theoretical/estimated statistical return[s]” to players. *Id.* at § 11.

true winnings.” Guidance § 1.1. To those ends, before granting an online gambling license, the Commission must verify that an operator is owned and controlled by “persons of integrity” and managed by “persons of integrity and competence.” OGRA § 4(2).⁸ The Commission retains authority to investigate after granting a license, including the right to inspect servers, and it has the power to suspend or terminate licenses. OGRA § 11–18.

To protect players, the Commission also approves and enforces the terms and conditions each licensee offers its customers. Guidance § 3.5.5. Players must be given an opportunity to review the terms, which should include a reference to specific game rules; a discussion of how disputes will be handled; procedures for dealing with “blatant or palpable errors, erroneous pricing, mistakes or omissions;” and limits on accounts, bets, and payouts. *Id.* And the games themselves must be technically certified by an approved testing facility to ensure that they are consistent with the stated rules and terms. Guidance § 3.5.9. The Commission also ensures that a licensee has adequate safeguards in place to protect players’ funds and to pay winnings; licensees must have “player protection arrangements” to “cover in value the

⁸ The Commission’s Inspectorate conducts due diligence on “each person connected with the application” for a license. Guidance § 3.5.1. Any company connected with the prospective licensee is also subject to the Inspectorate’s investigation, Guidance § 3.5.2, as are the prospective licensee’s accounts and business models, Guidance § 3.5.3, and any beneficial owners of the prospective licensee, Guidance § 3.5.4.

amount of money players have in their accounts plus any monies owed to them by the operator” Guidance § 3.5.8.

Licenseses must additionally comply with the IOM’s Criminal Justice Act, which requires them to adopt comprehensive customer identification, record keeping, reporting, staff training, and communication and control procedures to combat money laundering and terrorist financing.⁹ The strength of these regulations rates IOM alongside the U.S. by international standards.¹⁰

Finally, the IOM requires licenseses to combat problem gambling. Operators must exclude individuals under the age of 18 from registering to play. Guidance § 3.5.15. They must also implement mechanisms to exclude problem gamblers, such as robust self-exclusion mechanisms. Guidance §

⁹ For example, the Inspectorate reviews a licensee’s “know your customer,” anti-money laundering, and “countering the financing of terrorism” procedures. Guidance § 3.5.12. Additionally, licenseses must appoint a Money Laundering Reporting Officer with independent and unimpeded access to the licensee’s board or ownership. Criminal Justice (Money Laundering – Online Gambling) (No. 2) Code 2008, §§ 3, 16 (hereinafter “AML Code”); *accord* Special Rules for Casinos, 31 C.F.R. § 103.64 (requiring casinos to create compliance programs for preventing criminal activity). Enhanced scrutiny is triggered by certain activities, such as large cash withdrawals. AML Code § 7(3); *compare id.* with 31 C.F.R. § 103.21 (requiring casinos to report transactions “involv[ing] or aggregat[ing] at least \$5,000 in funds” that the casino has reason to suspect have, *inter alia*, “no business or apparent lawful purpose”).

¹⁰ For example, a recent audit similarly ranked IOM and the U.S. in terms of compliance with Financial Action Task Force (“FATF”) 40 + 9 recommendations. *Compare* Int’l Monetary Fund Legal Dep’t, *Isle of Man: Detailed Assessment Report on Anti-Money Laundering and Combating the Financing of Terrorism* 245–52 (Sept. 2009) with Fin. Action Task Force, *United States of America: Report on Observance of Standards and Codes* 11–15 (Sept. 2006), available at <http://www.imf.org/external/pubind.htm> (select “IMF Country Reports” and search by title).

3.5.15. Operators must also “fund education, research and support for problem gambling.” Guidance § 5.

B. Italy.

In 2007 Italy implemented a regulatory regime to govern Internet poker tournaments. Francois Peglau, GamblingCompliance Ltd., *Italy* 23 (Mar. 5, 2010) (hereinafter “Peglau,” attached as Ex. B). Under this law, Internet service providers are required to block access to gaming sites that lack valid licenses. *Id.* at 26. Regulation of gaming is delegated to the Amministrazione Autonoma Dei Monopoli Di Stato (“AAMS”), which licenses Internet poker site operators and must approve any new game they desire to offer. *Id.* License applicants must submit a “gaming platform plan,” which describes the computerized environment in which the game is played. *Id.* The platform must guarantee the “correctness, integrity, reliability, security, transparency, and confidentiality of the activities and functions performed and the correctness and timeliness of the payment of the winnings.” *Id.* The platform must also retain comprehensive data about gaming sessions for a minimum of five years, and be accessible to AAMS for monitoring and inspection. *Id.* Additionally, the platform must be connected to SOGEI (a centralized government computer network), to allow for real-time auditing and monitoring of gaming activity. *Id.* at 27. Operators must also submit to AAMS for review the rules of the games they offer, including

those governing the allocation of winnings, and a contingency plan for network malfunctions. *Id.*

Additional controls are being phased in, in accordance with more recent legislation. For example, operators will be required to combat problem gambling by, among other things, preventing minors from accessing games, implementing tools for the exclusion of problem gamblers and promoting responsible gaming measures. *Id.* at 35. Additionally, Internet service providers must prevent players from gambling with operators not in possession of an Italian license (those operators are “black-listed” by AAMS). *Id.* at 26. Finally, operators must implement anti-money laundering procedures, such as enhanced identity verification for transactions in excess of € 1000. *Id.* at 33.

C. France.

France recently established L’Autorité de régulation des jeux en ligne (“ARJEL”), an agency that licenses and regulates online gaming. Texte Adopté no. 438, April 6, 2010.¹¹ Licensed operators must be established or maintain a headquarters in the European Union or Economic Area—excluding tax havens, as identified by the Organization for Economic Cooperation and Development (“OECD”), and nations outside the reach of

¹¹ Available at <http://www.assemblee-nationale.fr>.

the EU's obligations of administrative cooperation and mutual assistance. They must also maintain bank accounts in France, *id.*, ch. III, art. 18, and locate in France a "front server" that stores data exchanged with players. The law imposes additional data archiving requirements, and obliges operators to provide French regulators access to the data. *Id.*, ch. X, art. 38. The French government will impose a licensing fee and a structured tax on operators and codify new sanctions for unlicensed operators. *Id.*, ch. X, art. 46; *id.*, ch. XII, art. 56, § 1; *see generally* Pat Rodrigue, GamblingCompliance Ltd., *France* 5–14 (Apr. 16, 2010) (attached as Ex. C).

D. The United Kingdom, Alderney and Gibraltar.

Under its Gambling Act of 2005, the U.K. extensively regulates Internet gaming, requiring, among other things, the rigorous inspection of license applicants and robust protections for children.¹² The U.K. also mandates strict anti-money laundering procedures.¹³ Likewise, Alderney, a British Crown Dependency, has a comprehensive regulatory structure for Internet gaming, as does Gibraltar, a British overseas territory.¹⁴

¹² *See generally* Gambling Act, 2005, ch. 19, available at http://www.opsi.gov.uk/acts/acts2005/ukpga_20050019_en_1.

¹³ *See, e.g.*, Gambling Commission, Conditions and Codes of Practice 8 (Dec. 2008) available at http://www.gamblingcommission.gov.uk/shared_content_areas/publications_2008/lccp_09_remote_betting.aspx.

¹⁴ Alderney's 2009 eGambling Regulations, available at <http://www.gamblingcontrol.org/userfiles/file/regulations.pdf>, set out, in nearly 300 pages of

E. United States.

The U.S. Congress is currently considering three bills that would license and regulate Internet poker. In February 2010, Senators Ron Wyden (D-OR) and Judd Gregg (R-NH), joined later by Senator Christopher Bond (R-MO), introduced the Bipartisan Tax Fairness and Simplification Act of 2010 (S. 3018), which would amend Title 31 of the United States Code to add a subchapter on “Regulation of Lawful Internet Gambling.” In its findings, the Bill states:

An effective Federal licensing system would ensure that licenses are issued only to Internet gambling operators which meet strict criteria to protect consumers, and which—

- (A) are in good financial and legal standing, and of good character, honesty, and integrity;
- (B) utilize appropriate technology to determine the age and location of users;
- (C) adopt and implement systems to protect minors and problem gamblers;
- (D) adopt and implement systems to enforce any applicable Federal, State, and

detail, requirements that provide for protection against money laundering and terrorist financing, see sched. 16; requirements for age and location verification, see pt. V, ch. V, reg. 227; and requirements for rigorous internal controls, see pt. V, ch. I, reg. 175. Gibraltar’s 2005 Gambling Act, available at <http://www.gra.gi/sites/gambling/downloads/42/gambling%20ord%202005.pdf>, requires, among other things, security measures for gaming technology, see pt. VI, § 25; privacy controls for customer information, see pt. VI, § 30; anti-money laundering and other crime controls, see pt. VI, § 33; and protections for minors, see pt. VII, § 37.

Indian tribe limitations on Internet gambling;
and

(E) have in place risk-based methods to identify and combat money laundering and fraud relating to Internet gambling, and to protect the privacy and security of users.

S. 3018, 111th Cong. § 425(a) (2010).

The bill establishes disclosure and eligibility requirements, and delegates licensing authority to the Secretary of the Treasury, who would also be empowered to pursue civil enforcement actions to assure compliance. *Id.* An applicant would be required to provide, among other things, its criminal history (if any), financial statements, documentation showing its corporate structure, and documentation containing “detailed evidence” of plans to comply with regulations—particularly those directed at the protection of underage and problem gamblers, fair operation of games, and law enforcement concerns. *Id.* The Secretary would be required to investigate applicants to ensure, inter alia, good character, honesty, and integrity. *Id.* The licensee must continue to meet these standards throughout the term of its license. It must also maintain mechanisms to ensure gamblers are of legal age and are playing from a jurisdiction where their wagers are legal, and to ensure that proper taxes are collected. *Id.*

A second bill pending in Congress, H.R. 2267, is cosponsored by two Representatives of the State of Washington. The Bill lays out a regulatory

scheme similar to S. 3018's, and includes a new criminal penalty for cheating—a fine and imprisonment for up to five years, H.R. 2267, 111th Cong. § 2(a) (2009). Finally, S. 1597, which was introduced by Senator Robert Menendez (D-NJ), would amend Title 31 to similar effect. *See generally* S. 1597, 111th Cong. (2009).

F. State Initiatives.

Both Florida and New Jersey are considering bills that would license, regulate and tax Internet poker. In Florida, HB 1441 would allow “hub operators” to incorporate within the state, associate themselves with existing card rooms, and offer Internet poker games to players present in the state and 21 or older. H.B. 1441 §§ 2(5)(b), 2(1)(k), 2(15), 2010 Reg. Sess. (Fla. 2010). Operators would be obliged to employ technology to, *inter alia*, verify players’ ages, combat problem gambling, assure network stability and security, and ensure fair gaming. *Id.* § 2(8). They would also be required to, among other things, implement a dispute resolution mechanism and anti-money laundering procedures. *Id.* Additionally, hub operators would be subject to extensive disclosure requirements and a \$500,000 bond to operate. *Id.* § 2(9); *see id.* § 2(8). Florida would impose a licensing fee and yearly revenue tax. *Id.* § 2(23).

New Jersey’s bill, S. 490, would license its in-state casinos to conduct Internet gaming operations. To obtain such a license, operators would need

to implement systems to ensure accurate age verification and user authentication, and to provide information security and assistance to problem gamblers, and they would have to locate their servers and other technology in Atlantic City. S. 490 §§ 6(6), 13, 214th Leg. (N.J. 2010), Like Florida, New Jersey would impose a license fee and yearly tax on revenues. *Id.* §§ 9, 27.

III. The State has offered no support for its claim that it is powerless to regulate Internet poker.

As robust regulation of online poker—more effective than in physical card rooms—is not only feasible but also a reality in a growing number of jurisdictions, it is no surprise that the State has failed to prove as a matter of law the bold assertion that such regulation is impossible.¹⁵

For the critical assertion that undergirds its position—that “[n]one of [its] normal regulatory safeguards can be effectively enforced” online—the State cites a single 1999 law review essay. State Br. 11 (citing Bruce P. Keller, *The Game’s the Same: Why Gambling in Cyberspace Violates Federal Law*, 108 Yale L. J. 1569 (1999)). But the State misreads the essay, which concludes that “there is no reason why existing gambling laws cannot be applied online as successfully as other laws have been.” Keller, *supra*, at

¹⁵ The State has not explicated the general problems of gambling with any detail or described their manifestation in the specific context of online gaming (let alone online poker). Similarly absent from the State’s pleadings is any discussion of the relevant technologies and controls available to the State. Indeed, the State has offered no particularized factual evidence whatsoever. Instead, it has relied upon vague and conclusory assertions, outdated academic articles and generic invocations of its police power.

1575; *see id.* at 1607 (arguing that gambling laws are “media-neutral and can be applied to Internet activity without the need for new models or legal regimes”). Indeed, the essay includes an entire Part that “emphasiz[es] how laws governing real space can be applied successfully to cyberspace in a media-neutral way.” *Id.* at 1575.¹⁶ Moreover, the essay obviously does not discuss the subsequent ten years of technological advances.¹⁷

The State asserts, without citation, that “[t]he solitary nature of Internet gambling exacerbates many of the problems traditionally associated with face-to-face gambling activities” and that “[t]he ‘virtual’ nature of Internet casinos . . . allows problem gamblers and other vulnerable individuals unlimited access to gambling activities without any restraint or limit, or possibility of intervention.” State Br. 12. But as explained above, the “virtual” nature of online gaming affords the State a remarkable opportunity—not present in its in-state card rooms—to suppress problem gambling by mandating timely intervention and mitigating restraints. And

¹⁶ The State’s confusion seems to stem from the essay’s focus on “gambling sites” that “operate from servers in foreign countries” and are “unsupervised by U.S. [and State] government regulators.” Keller, *supra*, at 1570; *see* State Br. 11 (discussing “enforce[ment] against off-shore Internet gambling operations”). But the fundamental thesis of the essay is that criminal prohibitions *can be enforced* against those operators, regardless of their physical location. *E.g.*, Keller, *supra*, at 1608 (“[I]t is difficult to comprehend why any new legal regime is necessary” to enforce prohibitions in light of internet technology).

¹⁷ When it was published, the Apple iPod was two years from market, and since then, Washington-based online-only retailer Amazon.com has increased its net sales more than twelvefold, becoming the hundredth-largest company in the United States.

contrary to the State's "assum[ption] that pathological or addictive gambling behaviors would be exacerbated by the increased opportunity to gamble at any time and from anywhere online," as a matter of fact, "research on this topic does not support this conclusion." Sparrow 12.

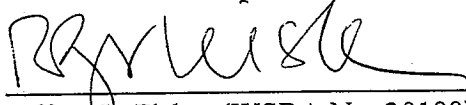
Finally, the State's claim that online gaming "is a magnet for organized crime, including traditional crime families and international terrorists," misses the mark. State Br. 12. As the State concedes, this is true of "forms of unregulated gambling." *Id.* at 11. But precisely the point is that online poker play need not remain unregulated.

The State's position begins and ends with a fallacy. It has repeated the claim that Internet poker cannot be regulated, but has offered no evidence to substantiate it. As demonstrated above, the State's claim is, in fact, untrue, and for that reason, the State's Commerce Clause defense is fatally flawed.

CONCLUSION

Despite the absence of a factual record, the State secured summary judgment—on the basis of unsupported assertions. This Court should vacate that judgment.

Respectfully submitted this 27th of April, 2010.



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EXHIBIT A

Can Internet Gambling Be Effectively Regulated? Managing the Risks

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TABLE OF CONTENTS

I.	OVERVIEW OF APPROACH AND SUMMARY OF RESULTS.....	1
A.	Our Approach.....	2
1.	Gambling by Minors.....	3
2.	Criminal and Fraudulent Behavior.....	3
3.	Network Access, Data Privacy and Security Issues.....	3
4.	Problem Gambling.....	4
B.	The Status Quo Offers No Effective Protection	4
C.	Legalization and Regulation Would Afford Significantly Better Protection than the Status Quo.....	6
D.	Regulatory Methods and Technologies for Controlling Each Type of Risk Already Exist.....	7
1.	Gambling by Minors.....	9
2.	Criminal and Fraudulent Behavior.....	9
3.	Network Access, Data Privacy and Security Issues.....	11
4.	Problem Gambling.....	12
E.	Conclusions.....	15
II.	REGULATORY METHODS AND TECHNOLOGIES AVAILABLE FOR CONTROLLING EACH RISK	16
A.	Gambling by Minors.....	16
1.	The Issue of Gambling by Minors	16
2.	Existing Controls in Other Jurisdictions	17
3.	Relevant Technologies for Risk Mitigation.....	20
4.	Conclusion	23
B.	Defrauding of Consumers by Site Operators	24
1.	The Issue of Fraud by Site Operators	24
2.	Existing Controls in Other Jurisdictions	26
3.	Relevant Technologies for Risk Mitigation.....	28
4.	Conclusion	29
C.	Cheating or Defrauding of Players by Other Players.....	29
1.	The Issue of Players Being Defrauded by Other Players.....	29
2.	Existing Controls in Other Jurisdictions	31
3.	Relevant Technologies for Risk Mitigation.....	32
4.	Conclusion	33
D.	Involvement of Organized Crime in Gambling Operations.....	33
1.	The Issue of Involvement of Organized Crime in Online Gambling.....	33

2.	Existing Controls in Other Jurisdictions.....	34
3.	Relevant Technologies for Risk Mitigation.....	36
4.	Conclusion	36
E.	Money Laundering by Players.....	37
1.	The Issue of Money Laundering by Players	37
2.	Existing Controls in Other Jurisdictions.....	39
3.	Relevant Technologies for Risk Mitigation.....	40
4.	Conclusion	42
F.	Money Laundering by Site Operators.....	43
1.	The Issue of Money Laundering by Site Operators.....	43
2.	Existing Controls in Other Jurisdictions.....	44
3.	Relevant Technologies for Risk Mitigation.....	44
4.	Conclusion	45
G.	Violation of Jurisdictional Restrictions or Prohibitions.....	45
1.	The Issue of Violation of Jurisdictional Restrictions.....	45
2.	Regulatory Strategy	46
3.	Relevant Technologies for Risk Mitigation.....	47
4.	Conclusion	49
H.	Breaches of Data Confidentiality.....	50
1.	The Issue of Data Confidentiality	50
2.	Existing Controls in Other Jurisdictions.....	51
3.	Relevant Technologies for Risk Mitigation.....	52
4.	Conclusion	53
I.	Communications and Computer Security Failures	53
1.	The Issue of Communications and Computer Security Failures.....	53
2.	Existing Controls in Other Jurisdictions	55
3.	Relevant Technologies for Risk Mitigation.....	56
4.	Conclusion	58
J.	Problem Gambling.....	59
1.	Problem Gambling.....	59
III.	SPECIAL ATTENTION TO PROBLEM GAMBLING.....	60
A.	Introduction.....	60
B.	What is Problem Gambling?.....	60
1.	Terminology.....	60
2.	Prevalence Rates and Trends	61
C.	Potential Effects of Legalization of Online Gambling on Problem Gambling.....	62
1.	Potential Adverse Effects of Legalization	63

2.	Potential Benefits of Legalization.....	69
D.	Concluding Remarks.....	72

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EXECUTIVE SUMMARY

This study was commissioned by Wired Safety, an Internet Safety and Educational charity. It examines a range of harms potentially associated with online gambling, and alternative methods for mitigating or minimizing them. Recognizing that the current U.S. prohibitionist regime with respect to online gambling is largely ineffective in achieving its aims, and provides no platform or opportunity for the implementation of most of the relevant harm-reduction strategies, we find that an alternative regime of legalization and regulation of online gambling would likely improve consumer welfare and protections. The body of this report evaluates a range of strategies, both regulatory and technological, that could be used to mitigate potential harms associated with online gambling more effectively.

Notwithstanding the current prohibitionist legal and regulatory approach, millions of U.S. residents gamble online through offshore gambling sites. As a result, the United States finds itself in the unfortunate position of incurring all the social costs of online gambling while having no control over the gaming sites that serve U.S. residents. The United States cannot disqualify industry participants from competing effectively for U.S.-based customers or offer its residents any consumer protections. Nearly all states permit some form of commercial gambling, and the industry is large and well-established. Clearly, policymakers have extensive precedent from which to draw strategies to mitigate the potential social harms of gambling.

Although some controls used in bricks-and-mortar casinos may not translate well to online gambling, several of the risks we examined become *more* amenable to control online. New technologies can be effective, even for those risks that are more difficult to address online. For example, geolocation and age verification technologies can help turn potentially significant risks into manageable ones.

In this study, we analyze 10 specific risks that others have suggested are potentially associated with online gambling: gambling by minors, fraud by operators, fraud by players, organized crime, money laundering by players, money laundering by operators, violation of jurisdictional prohibitions, breaches of data confidentiality, lack of site security, and problem gambling. It is important that regulators treat each of these potential risks differently. For some risks (such as players cheating other players), the public interest and the interests of the gaming industry align, making a cooperative regulatory relationship natural. For others (such as those involving potentially criminal conduct by operators), a strict enforcement regime would be more appropriate. Still other potential risks (such as underage and problem gambling) call for a more nuanced regulatory approach involving a mixture of strict enforcement, effective nonprofit support, community education, and cooperation, in keeping with the more complex motivations and incentives facing site operators.

For each of the 10 risks, we examined a set of regulatory methods and technologies that would provide a reasonable degree of risk management in a regulated environment. Most of these methods have already been implemented in some form in other jurisdictions. The United Kingdom, Alderney, Gibraltar, and others have successfully implemented

regulation, and nearly all of the well-regulated jurisdictions we studied address the 10 risks to some degree.

The establishment of a well-regulated industry under U.S. jurisdiction would offer far better protection against online gambling's potential social harms than outright prohibition. Combining a thoughtful regulatory scheme with education, technology tools, and support appears to be the most effective means of handling the realities and risks of online gambling in the United States. Therefore, we recommend that plans for regulating online gambling include the design and use of different risk-management strategies tailored to the different classes of risk that are associated with Internet gambling. In the end, consumers in the United States would be better protected than they are now.

I. OVERVIEW OF APPROACH AND SUMMARY OF RESULTS

Congress is debating legislation that would remove the existing prohibition on the use of the Internet for most types of gambling.¹ The proposed legalization of online gambling would be conditioned on the imposition of regulation designed to limit or prevent potential harms such as underage gambling, money laundering, and problem gambling.

A key issue in the debate over legalization of online gambling is whether regulation and technology could effectively control such potential harms. Some of the opposition to legalization reflects a perception that online gambling—in contrast to gambling in bricks-and-mortar casinos—would be difficult, if not impossible, to regulate effectively.

This study reviews the research literature and international approaches to online gambling. WiredSafety (the Internet safety and educational charity) has commissioned this study to help inform the legalization debate and to help educate the public on the risks associated with online gambling and the best ways to address those risks.²

We note that our expertise is in regulatory policy and its relationship to risk analysis, rather than in any extensive prior knowledge of the gaming industry and gambling behavior per se. We have critically reviewed the existing literature, evaluated relevant technologies, and interviewed a range of scholars and practitioner experts, both here and abroad. We have not, however, conducted any new epidemiological studies or field research. Our distinctive contribution is the frame for risk management and regulatory analysis, rather than any new scientific inquiry.

Our analysis does not directly address whether online gambling should be legalized. In focusing on managing risks, we did not weigh moral or religious objections to gambling, nor did we examine broadly libertarian arguments in favor of allowing adults to engage in pastimes they may enjoy. We did not conduct any analysis to quantify the benefits of potential tax revenues attributable to regulated online gambling. Further, we have not focused on any issues of federalism or on exactly where regulations and laws should fit into the U.S. multijurisdictional

¹ Internet Gambling Regulation, Consumer Protection, and Enforcement Act, H.R. 2267, 111th Cong. (2009), http://www.house.gov/apps/list/press/financialsvcs_dem/21frank_008_xml.pdf (last accessed on July 23, 2009), and Internet Gambling Regulation and Tax Enforcement Act of 2009, H.R. 2268, 111th Cong. (2009), http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h2268ih.txt.pdf (last accessed on August 28, 2009).

² This study was commissioned by WiredSafety.org, a 501(c)(3) charity and the largest and oldest online safety, education, and help group in the world. Originating in 1995 as a group of volunteers rating websites, it now provides one-to-one help, extensive information, and education to cyberspace users of all ages on a myriad of Internet and interactive technology safety issues. WiredSafety works in four major areas: help for online victims of cybercrime and harassment; assisting law enforcement worldwide on preventing and investigating cybercrimes; education; and providing information on all aspects of online safety, privacy and security. WiredSafety also has a longstanding interest in gambling policy and the prevention of underage gambling. The study was sponsored by Harrah's Operating Company, Inc and the Poker Player Alliance, who share many of WiredSafety's concerns. While the sponsors have provided valuable input into the framing of the research, the final decisions regarding the research approach and the final written product was solely made by the authors of the study, following consultation with WiredSafety, ensuring that the study was independent.

governance structure. Instead, we concentrated more narrowly on the obligations of government to protect citizens in general, and vulnerable groups of citizens in particular, from unnecessary exposure to harm.

We sought (1) to identify the specific risks that are associated with, or perceived to be associated with, Internet gambling; (2) to determine suitable regulatory strategies for controlling or managing those risks; and (3) to assess how effective those strategies are likely to be. We identified 10 distinct risks that fall into four broad categories. Those categories are as follows:

- Gambling by minors
- Criminal and fraudulent behavior
- Network access, data privacy and security
- Problem gambling

On the basis of our review of the existing literature and interviews with academics, regulators, industry participants, and public interest advocates, we came to the following conclusions:

- Online gambling could be regulated effectively if it were legalized.
- A well-structured regulatory regime should provide much better social and consumer protections than the status quo for the risks we identified.
- At a minimum, even an imperfect legalization and regulatory regime for online gambling would give Americans much more protection than they have now. The current prohibitionist policy is extremely weak: large numbers of U.S. residents already gamble online, but they do so using offshore sites, many of which are poorly regulated or unregulated.

For each of the 10 risks we examined, a set of regulatory methods and technologies exist that would provide a reasonable degree of control, and most of them have been implemented effectively in other jurisdictions or in other online settings.

Although some controls used in the bricks-and-mortar environment may not translate to online gambling environments, several of the risks we examined become *more* amenable to control online. Comprehensive electronic records and the ability to track financial transactions and betting patterns provide more opportunities for analysis and audit, and hence improve the chances of discovering fraud or criminal activity. They also allow gambling websites to provide tools to mitigate problem gambling in a timely manner.

A. Our Approach

Our approach has been to identify the specific risks that are perceived to be associated with Internet gambling and then to determine how best to control or manage them. Those risks are described below.

1. **Gambling by Minors**

- a. Gambling by minors: There is concern that minors might find it easier to access and use online gambling services in a legalized environment.

2. **Criminal and Fraudulent Behavior**

- a. Defrauding of consumers by site operators: There is the possibility that online site operators may be more likely than their bricks-and-mortar counterparts to rig games, refuse to pay out winnings, or simply vanish, taking with them players' account balances.
- b. Cheating or defrauding of players by other players: There is a concern that players could collude to defraud others, particularly in online poker. Online gambling may offer opportunities for collusion that are not available in a physical environment with visual surveillance.
- c. Involvement of organized crime in gambling operations: Organized crime has a history of involvement with the bricks-and-mortar casinos and is now involved in some online commerce. There is some concern that involvement in the online gambling industry may be a natural next step.
- d. Money laundering by players: There is concern that players or groups of players acting in concert could use legitimate gambling operations for money laundering.
- e. Money laundering by site operators: The possibility has been raised that site operators could use online gambling operations, with its significant financial flows, as a cover for money laundering on a large scale.

3. **Network Access, Data Privacy and Security Issues**

- a. Violation of jurisdictional restrictions or prohibitions: Government at the state, local, and tribal levels has traditionally exercised control over gambling within a given jurisdiction. The advent of the Internet has opened the question as to whether controls mandated by any proposed laws can be enforced within particular jurisdictions.
- b. Breaches of data confidentiality: To register for play, players surrender personal or financial data to site operators. Consumers might be harmed by deliberate or accidental breaches of the confidentiality of those data.

- c. Communications and computer security failures: Some are concerned that site operators might not use appropriate security practices, procedures, and technologies to ensure the integrity of their sites, the gaming on those sites, and player interactions. Absent proper security measures, malicious code could be transmitted to players, game operations could be infiltrated, and intrusions into the systems could compromise the game play and security of users.

4. Problem Gambling

- a. Problem gambling behaviors: Some argue that increased opportunity to gamble at any time, from anywhere, and at a faster pace might exacerbate pathological, addictive, or problem gambling behaviors.

With respect to each of these four categories of risks, we sought to answer three broad questions:

- (1) In the existing prohibitionist legal and regulatory regime, what level of protection are U.S. consumers afforded?
- (2) With legalization, could these risks be addressed more effectively than they are now, and assuming legalization, what regulatory strategy is best suited for addressing these risks?
- (3) What are the potentially relevant technologies and methods available for effective risk mitigation, and how might other parties contribute toward effective control?

Our answer to the threshold question of whether online gambling can be effectively regulated came out of our analysis of these more specific questions.

B. The Status Quo Offers No Effective Protection

Many U.S. residents already use online gambling services despite statutory restrictions. Recent estimates indicate that U.S. gamblers constitute roughly one-fourth to one-third of the global market for online gambling services.³ The size of the U.S. share of that global market was estimated to be \$5.9 billion in 2008.⁴

³ G. Srinivasan, "EU Slams US on Its Remote Gambling, Betting Laws," *Business Line*, June 14, 2009, <http://www.thehindubusinessline.com/2009/06/14/stories/2009061450870400.htm> (last accessed on September 10, 2009). Also noted in an August 4, 2009 interview with Simon Holliday, Director of H2 Gambling Capital (U.K.). Also see Simon Holliday *et al.*, *Internet Gambling Market Overview: AGA Internet Gaming Task Force*, H2 Gambling Capital, December 2, 2008, p. 8.

⁴ From H2 Gambling Capital, cited in American Gaming Association, *Internet Gambling*, AGA Fact Sheet, (continued...)

The mainstay of the current prohibitionist regulatory structure is the Unlawful Internet Gambling Enforcement Act (UIGEA). Instead of criminalizing gambling itself, the UIGEA was intended to prevent U.S. residents from gambling by placing restrictions on the role of financial institutions in transmitting payments to and from gaming operators. However, because workarounds such as e-wallets (essentially a payment processor situated between banks and gambling sites), phone-based deposits, and prepaid credit cards have proliferated, very few U.S.-based gamblers are presently much inconvenienced.⁵ Most gamblers are either unaware of or confused by the patchwork of federal and state restrictions, and many are readily guided by unregulated online gambling sites toward financial mechanisms that they can use to make deposits and withdrawals.⁶

The net effect is that the U.S. attempt to prohibit online gambling has instead pushed it offshore. Sites are readily available to U.S. residents through the essentially borderless medium of the Internet. Some sites are well-regulated, such as those based in the United Kingdom, Alderney, and Gibraltar, and others are less-well-regulated or unregulated, such as those in Antigua, Grenada, or the Kahnawake Mohawk territory. (Of course, it is the less-well-regulated international sites that provide easier access to U.S. consumers.) As a result of the global gaming industry's adaptations to the U.S. strategy, the United States finds itself in the unfortunate position of

- incurring all the social costs related to U.S. residents' online gambling;
- exercising no jurisdiction or control over the gaming sites that serve U.S. residents;
- being unable to offer U.S. residents who choose to gamble on overseas sites any consumer protections or to implement any other harm-reducing strategies; and
- being unable to qualify industry participants or even exclude criminal groups from competing for U.S.-based customers.

In an effort to address this reality and enforce current restrictions more aggressively, federal officials recently instructed four banks to freeze accounts belonging to online payment processors. The frozen accounts apparently contained funds owed to some 27,000 people who used offshore poker websites.⁷ Such financially based efforts seem to have had only a temporary

http://www.americangaming.org/Industry/factsheets/issues_detail.cfv?id=17 (last accessed on August 27, 2009).

⁵ USAplayers.com, *USA Poker Deposit Methods*, <http://www.usaplayers.com/poker/deposit-methods/index.html> (last accessed on August 8, 2009), and USAplayers.com, *Online Poker Deposits and the UIGEA*, <http://www.usaplayers.com/deposit-methods/articles/poker/online-poker-deposits-and-the-uigea.html> (last accessed on August 8, 2009).

⁶ Bo Bernhard *et al.*, *Internet Gambling in Nevada*, University of Nevada, Las Vegas, April 2007, at p. 26. Also see, Gilbert M. Gaul, "Players Gamble on Honesty, Security of Internet Betting," *The Washington Post*, November 30, 2008, p. A12.

⁷ Tamara Audi, "U.S. Deals Blow to Online-Poker Players," *The Wall Street Journal*, June 10, 2009, <http://online.wsj.com/article/SB124459561862800591.html> (last accessed on August 3, 2009).

chilling effect.⁸ Over the long run, it is probably not feasible for the federal government to prevent U.S. residents from accessing foreign sites via the Internet. Unlike China or Iran, for example, the United States has displayed no appetite for centralized control of the Internet to block citizens' access to undesirable sites.

Nor would criminalization of the gambling itself be an effective strategy.⁹ First, it would likely generate a massive pool of lawbreakers, almost none of whom would make attractive targets for criminal prosecution—because it would likely be a waste of law enforcement resources to pursue individual online gamblers. Second, it would exacerbate the dangers of consumer fraud at online gambling sites by making aggrieved consumers more reluctant to report their experiences.

C. Legalization and Regulation Would Afford Significantly Better Protection than the Status Quo

At a minimum, legalization and regulation of online gambling would give Americans much more protection than does the current prohibitionist regulatory framework. Although the kind of regulation that would accompany legalization would not be failsafe, it would be a significant improvement over the current regulatory and enforcement structure. We believe that safeguards could be implemented that would, on balance, substantially improve protections against the identified risks. These safeguards would also provide protection equal to or greater than that provided within the U.S.-based bricks-and-mortar gambling industry. We recognize that no set of technical or regulatory controls could ever eliminate these risks entirely. But even if the new fence had a few holes, it would be an improvement over having no fence at all.

The view that online gambling, in contrast to its bricks-and-mortar casino counterpart, is impossible to regulate reflects an old-fashioned perception of cyber jurisdictional authority. Many offshore commercial entities that operate online are subject to U.S. legal jurisdiction under existing long-arm statutes and authority. When coupled with governmental licensing authority, the ability to police online activities is even more powerful. Legalization with regulation would provide U.S. authorities with the power to grant or deny licenses and to impose significant sanctions on noncompliant licensees. Those licenses would be highly valuable to site operators. Compliance with any regulatory requirements and strict licensing conditions that Congress chooses to impose in return for the privilege of the license would therefore become a cost of doing business.

⁸ Noted in an August 4, 2009 interview with Simon Holliday, Director of H2 Gambling Capital (U.K.).

⁹ Ryan S. Landes, "Layovers and Cargo Ships: The Prohibition of Internet Gambling and a Proposed System of Regulation," *New York University Law Review*, 82 (May 2007): 913–943, at p. 927–936. Also see Gerd Alexander, "The U.S. on Tilt: Why the Unlawful Internet Gambling Enforcement Act Is a Bad Bet," *Duke Law & Technology Review*, No. 5 (2008), at ¶44. Also see Roger Clarke and Gillian Dempsey, "The Feasibility of Regulating Gambling on the Internet," *Managerial and Decision Economics*, 22 (2001): 125–132, at p. 130. Also see Testimony of John Lyons, in U.S. House of Representatives, Committee on the Judiciary, *Establishing Consistent Enforcement Policies in the Context of Online Wagers*, 110th Cong., 1st Session, November 14, 2007, p. 107.

Just as with bricks-and-mortar casinos, the requirement for site operators to maintain a license gives the government the ability to exclude bad actors as well as impose a broad array of conditions for, and oversight of, licensees. In contrast, the current prohibitionist policy is extremely ineffective: large numbers of U.S. residents already gamble online, but they do so using offshore sites, many of which are poorly regulated.¹⁰ With legalization, we would expect that most online gamblers would prefer licensed U.S.-based sites because of their integrity and security, rather than accept the risks posed by unregulated or poorly regulated sites. A well-structured regulatory regime would provide better protections against all of the risks we identified.

This conclusion is supported by the experience of other jurisdictions in regulating online gambling. Some of these, such as the United Kingdom and Alderney, have adopted regulatory regimes that appear to provide protection against the identified risks. That may be the most compelling evidence that online gambling can be effectively regulated.

D. Regulatory Methods and Technologies for Controlling Each Type of Risk Already Exist

For each of the 10 risks we examined, a set of regulatory methods and technologies already exists that would provide a reasonable degree of risk management. Moreover, most of them have been implemented in other countries. One general insight from regulatory policy, and a review of other country's experiences, is that no one size fits all: regulators should treat different risks differently. The incentives and motivations of different parties vary across risk categories, as does the locus for detection and control interventions. Understanding the natural incentives of the gaming industry with respect to each class of risk reveals whether a cooperative regulatory strategy would likely be more effective than a traditional enforcement-centric one.

For example, for at least one of the risks we identified (protecting the integrity of poker games by preventing players from colluding or conspiring to cheat other players), the interests of the public and of the gaming industry align reasonably closely. Both groups are interested in ensuring the integrity of the games. That makes a more cooperative and less adversarial regulatory relationship quite natural.

For other risks (such as defrauding of consumers by site operators, involvement of organized crime, and money laundering by site operators), a strict enforcement regime focused on identification and rapid exclusion of bad actors is more obviously appropriate. Oversight in these areas would focus heavily on up-front qualification or "suitability" to exclude those with criminal histories or connections and persons otherwise lacking in "good character, honesty, and integrity" as is the case in the bricks-and-mortar space. Enforcement activity would focus on bad actors, with the goal of exclusion and sanction. The intense and strict monitoring regime for reputable sites would include provisions designed to prevent or reveal any infiltration over time

¹⁰ G. Srinivasan, "EU Slams US on Its Remote Gambling, Betting Laws," *Business Line*, June 14, 2009, <http://www.thehindubusinessline.com/2009/06/14/stories/2009061450870400.htm> (last accessed on June 30, 2009). Also see *Supra* at footnote 7.

by undesirable groups or influences. Such regulations would mirror those now in place for bricks-and-mortar casinos.

Reputable sites, whose competitive advantage lies substantially with their reputation for integrity, would not be much troubled by the type of oversight designed to keep the “good character, honesty, and integrity” bar for admission high and the bad players out. In fact, they should appreciate such oversight as a positive contribution to the overall public perception of their industry, and the regulatory certainty provided by a licensing model would help with the industry’s overall long-term planning.¹¹

Some risks (gambling by minors, money laundering by players, problem gambling, breaches of data confidentiality, and lack of site and technology security) present more complex challenges in terms of regulatory design. If site operators were driven solely by their short-run economic incentives, they would more likely take bets from minors, problem gamblers, and money launderers (because the sites gain financially, at least in the short run, from all such bets), and they might limit their investments in data privacy and security. Site operators might also gain, in the short run, from abusing or selling personal and financial data provided to them by gamblers.

In the longer term, of course, site operators value their brand names and reputations matter, and these five risks all figure as *reputational risks* from the industry’s perspective just as they do in the bricks-and-mortar gambling industry. By setting the admission bar for licensees suitably high, U.S. regulators would intend to admit only reputable operators, whose behaviors would be guided by the value they place on establishing and maintaining a trusted brand. This is the approach taken by regulators in other jurisdictions—license only reputable firms. Probity investigations are conducted into the companies and their associates before a license is issued.¹² Hence, for these five risks, close supervision would be required if an operator were regarded as a rational but short-sighted actor. At the same time, a more cooperative and symbiotic regulatory relationship ought to emerge when reputable operators take a longer-term, strategic view. To better align site operators’ short- and long-term interests, regulation also would provide for sanctions, from monetary fines up to and including loss of license for those site operators that choose to disregard mandated operational and consumer protections.

One strategy to provide longer-term, reputation-based incentives for good behavior is to create costs to entry—through the regulatory process, licensing fees, or other means—that reduce

¹¹ Noted in an August 13, 2009 correspondence with Katharina Riedl of bwin (Austria).

¹² Noted in an interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority and an interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia). Also, as noted in an August 31, 2009 correspondence with John Sealy, Manager of Information Systems and Technology Services at the Licensing, Regulation and Alcohol Strategy Division of the Northern Territory Department of Justice (Australia), licensees often wish to be seen as responsible and as good corporate citizens. Also see Testimony of André Wilsenach and Testimony of Mary Williams, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, p. 122 and 140.

incentives to make a quick profit and leave the industry. For all risks created by operator shortsightedness, regulators need to establish and retain sufficient audit and monitoring systems so they can see when organizations that are otherwise reputable tilt too heavily toward short-term gain at the expense of public protection. Regulators should not accept the industry's protestations that they can be entirely trusted to take care of such risks without oversight simply because it is in their interest to do so. It is indeed in the industry's long-term interests to do so, but short-term considerations sometimes prevail, even in major corporations and multibillion dollar industries.

The following sections of this study describe a variety of control technologies and regulatory tactics relevant to each risk, and identify the most promising approaches in each case. Table 1, in Appendix A, lists the 10 risks and for each outlines

- the level of protection afforded under the current regime (column 2);
- the overall structure and style of regulatory oversight most natural for each risk (column 3), and
- some key points regarding relevant technologies and control strategies (column 4).

Below we summarize key points in relation to each risk.

1. Gambling by Minors

There is a general concern that underage gamblers may access or attempt to access online gambling sites.

- Gambling by minors: A number of technologies routinely used in other industries can be used to exclude minors from online gambling, including a variety of data-matching techniques, electronic or other submission of documentary evidence of age, and possibly application of biometric identification systems. The strongest form of control would require positive matching of a player at the time of registration against existing databases of known adults, thus excluding minors, as well as identity-verification prior to initiating any session of play. U.S.-licensed operators would be expected to use filters and procedures that are as discriminating as reasonably possible. With respect to U.S. residents, we would expect available data needed for age-verification to be of high quality and reliability. Site operators could also be required to provide child-protective software to parents to help prevent minors from accessing gambling sites. Alternatively, a separate governmental or nonprofit entity could provide such software.

2. Criminal and Fraudulent Behavior

Criminal activity can stem from site operators or the players themselves. The following risks are related to criminal activity by site operators:

- Defrauding of consumers by site operators,
- Involvement of organized crime in gambling operations, and
- Money laundering by site operators.

These risks would be effectively limited by a regulatory strategy designed to keep the bar for admission high and to keep criminals out. Such controls have worked well in bricks-and-mortar casinos and would operate similarly with U.S.-licensed online site operators. Relevant tactics include rigorous vetting procedures for new applicants and monitoring of licensed site operator behavior to prevent or detect regulatory noncompliance, criminal conduct, fraudulent and deceptive practices, and disregard for consumers' rights.

Regulatory strategy with respect to these risks would be enforcement-centric with a focus on excluding operators with criminal histories or connections. Reputable site operators with brands to protect could not afford to risk damage to their reputations, loss of their licenses, or regulatory sanctions. Thus, we would expect the industry at large to support the type of demanding admission standards, regulatory monitoring, and sanctions designed to keep bad actors out of the business. Players, best positioned to detect improper conduct or consumer fraud by site operators, would be enabled and encouraged to report site operators' improper conduct directly to regulators and others in law enforcement. Players would also have access to U.S. courts for dispute resolution.

Player criminal behavior falls into two major categories—cheating or defrauding of players by other players and money laundering by players.

- Cheating or defrauding of players by other players: Most of the cases of improper player collusion or cheating that have come to light have been detected by other players. With a regulator in place for U.S.-licensed sites, players would have stronger recourse against the sites, or against other players, by lodging complaints with the regulator or relevant law enforcement agencies. More important, licensed operators could be required to maintain comprehensive databases of all betting transactions and these databases could be examined and analyzed by regulators in the event of an inquiry or the triggering of red flags. Site operators, who themselves have a strong interest in maintaining the integrity of their games, could be expected or even required to implement pattern recognition software to scan routinely for anomalous betting patterns.
- Money laundering by players: Online gambling operators, like operators of bricks-and-mortar casinos, would be subject to current anti-money-laundering regulations. These regulations would require site operators to expend some level of effort in detecting money laundering. The online environment provides *better* opportunities for detecting money laundering by players or player groups than the bricks-and-mortar casino environment. Site operators could be required to retain comprehensive data on all deposits, withdrawals, and betting transactions and to make these data available to regulators for examination and analysis. Given complete data, most patterns related to money laundering (such as light betting or

matched bets placed by collaborators) would be easier to detect than they are in a physical environment (where complete transaction histories are available only in the form of video recordings). Software that detects anomalies and suspicious behaviors could be operated easily and routinely on digital databases by the site operators, by regulators, or by both. The site operators' obligations with respect to their own detection of money laundering would form a part of their ordinary compliance obligations under the licensing regime.

3. Network Access, Data Privacy and Security Issues

Any U.S. legalization and regulatory regime would likely address the risk of access to online gambling sites from jurisdictions that prohibit such activity.

- Violation of jurisdictional restrictions or prohibitions: State, local, and tribal governments may continue to prohibit or restrict (1) the operation of gambling sites from within their jurisdictions and (2) online gambling by individuals resident or physically present within their jurisdiction. Licensed U.S. sites could be required to take all reasonable steps not to permit registration or participation by individuals in such states. A range of geolocation technologies are now available, mostly tied to identification of the user location by reference to their IP addresses. Such technologies, while not entirely foolproof, have the capability of reducing risks as much as is required by regulators. IP geolocation, together with address verification at registration and other controls, can be expected to deter the bulk of casual attempts to gamble from within restricted states. Determined users, of course, already have access to foreign sites and would probably continue to use those rather than go to the trouble of devising sophisticated technological means for defeating U.S.-based geolocation controls. Regulatory oversight methods could include audits of U.S.-based operators' software controls and routine "mystery shopping" at U.S. sites conducted from locations within states that had chosen to exercise their rights to restrict online gambling.

Data privacy and security risks include: sites not using commercially appropriate security systems and practices; intentional or accidental breach of the gambling site's and user's data security; and the introduction of spyware, adware, or malicious code into gambling websites' software or transmission of such malware to users' computers.

- Breaches of data confidentiality: Under legalization and regulation, U.S.-licensed operators would be subject to all applicable federal and state requirements regarding data confidentiality and security. Site operators would be subject to regulatory and potentially criminal sanctions and civil liability for any breaches or abuses of personal or financial data. Their data-protection controls would be subject to regulatory audit. There is no reason to believe that licensed online gambling operators would be any less able or willing to fulfill these obligations than other online merchants with similar data custody obligations.
- Communications and computer security failures: Under the current regime, U.S. authorities have no oversight over security for online gambling sites. With

legalization and regulation U.S. licensed sites would be subject to existing data protection laws. Furthermore, U.S. regulators would have an opportunity to require state-of-the-art cybersecurity controls to protect against the introduction of malicious code or the unauthorized manipulation of games.

4. Problem Gambling

It is relatively easy to demonstrate for the other risk categories that a well-structured regulatory regime coupled with relevant technologies should provide better protection than the status quo. For problem gambling, however, the potential effect of legalization is less obvious a priori. Many might assume that pathological or addictive gambling behaviors would be exacerbated by the increased opportunity to gamble at any time and from anywhere online. But research on this topic does not support this conclusion. In particular, the link between the availability of online gambling and increases in the prevalence of problem gambling has not been established. Nevertheless, some online gamblers would be problem gamblers.

In a well-regulated online environment, gamblers could have opportunities and technologies made available to them to help curb addictive or problematic gambling behaviors. Such mechanisms would permit them to limit their gambling volume, deposit rates, loss rates, and the size of each wager. Users could also access online clinical and self-help resources from links provided at the gambling site.

The relationship between legalization and potential effects on problem gambling rates must certainly be examined carefully. Opponents of legalization fear an increase in problem gambling rates. However, gambling experts in the United States and the United Kingdom have reported that the prevalence rates for pathological gambling have remained static and low (roughly 0.7% of the adult population, in both countries) for many years. A large-scale study of gambling prevalence in the U.K. found the 0.7% rate remaining stable from 1999 through 2007 despite substantial increases in gambling opportunities during this period.¹³

Because this issue is likely to receive considerable attention as the United States considers legalization, we have attempted to analyze the various arguments given as to why the act of legalization might drive the level of problem gambling up or down. We have identified five popularly discussed mechanisms through which legalization could drive problem gambling up, and describe them here along with some observations that help mitigate the anticipated effects:

- Mechanism: Inhibitions to gamble that are based on would-be gamblers' knowledge of current legal restrictions would be removed.

¹³ Noted in a June 10, 2009 interview with Howard Shaffer, Director of the Division on Addictions and Associate Professor of Psychology in the Department of Psychiatry at the Cambridge Health Alliance. Also see Jacob Sullum, "Some Bets Are Off: The Strangely Selective and Self-defeating Crackdown on Internet Gambling," *reasononline*, June 2008, <http://www.reason.com/news/show/126022.html> (last accessed on September 10, 2009). Also see Heather Wardle *et al.*, *British Gambling Prevalence Survey 2007*, National Centre for Social Research, Prepared for the Gambling Commission, September 2007, <http://www.gamblingcommission.gov.uk/pdf/British%20Gambling%20Prevalence%20Survey%2007%20-%20Sept%202007.pdf> (last accessed on September 10, 2009), p. 10.

- ❖ Observation: Gamblers in the United States are generally ignorant of or completely confused about existing legal restrictions, and (until very recently) there has been no enforcement against the gamblers themselves.¹⁴ Hence, the lifting of the prohibition itself is unlikely to have any significant impact on would-be gamblers' willingness to gamble online.
- Mechanism: Gamblers may be more comfortable gambling online because licensed operators are reputed to be trustworthy.
- ❖ Observation: The gamblers most likely to be influenced by the availability of trusted brand-name sites are those who gamble already, perhaps in the casino environment, and hence know the brands. Knowledgeable gamblers may indeed shift their business, but this represents displacement, not overall growth. And the displacement would be from bricks-and-mortar to online gambling, which can offer many more options and protections for problem gamblers than can land-based casinos.
- Mechanism: Gambling opportunities would be ubiquitous and available 24/7.
- ❖ Observation: U.S. residents already have online gambling options available to them all day, everyday, and from anywhere. So the addition of U.S.-licensed sites would not alter that particular reality.
- Mechanism: Lifting the UIGEA's restrictions on financial transactions might make it easier for consumers to place bets online.
- ❖ Observation: Lifting the restrictions of the UIGEA would not make it significantly easier for U.S. residents to make deposits to online sites. Enough workarounds have been designed, and are energetically promoted to consumers by the offshore sites, to render the existing restrictions largely ineffective.¹⁵
- Mechanism: Advertising by licensed online gambling sites might lead to increased problem gambling.
- ❖ Observation: Although advertising is one avenue for the expected increase in online gambling that would follow legalization, little evidence exists to show whether and to what extent advertising-induced growth in, or redistribution of, gambling volume might produce increases in problem

¹⁴ The recent seizure of online poker players' funds was termed an "unprecedented action" by the Poker Players Alliance. See *Supra* at footnote 7.

¹⁵ See *Supra* at footnote 5.

gambling rates.¹⁶ Furthermore, this mechanism (allowing advertising for online gambling sites) is controllable to the extent deemed necessary or desirable, through regulatory restriction.

We also looked at two mechanisms through which legalization and regulation could drive problem gambling *down*:

- Mechanism: Tax and license-fee revenue distributions may provide an opportunity to extend and enhance counseling, treatment, and support programs for problem gamblers.
 - ❖ Observation: Significant tax revenues might be anticipated from U.S. operators, and revenue distributions from taxes and license fees could substantially boost publicly funded prevention, counseling, and treatment programs, as well as research on gambling addiction. Existing budgets for counseling and treatment services for problem gamblers have been limited, and most health insurance programs do not currently cover these services.¹⁷
- Mechanism: Regulators could require licensed domestic sites to lead the world in offering a full suite of advice and protections for problem gamblers to an even greater extent than is the case in bricks-and-mortar casinos.
 - ❖ Observation: U.S.-licensed sites could be required to display offers of help prominently on their websites, including (1) registration pages that offer self-diagnostic tests designed to help would-be gamblers understand their own attitudes and vulnerabilities; (2) web pages that display prominent links to support and counseling services; and (3) availability of speed-of-play, compulsory time-outs, or player-loss-rate caps. All players should be offered the opportunity up front and at subsequent intervals to voluntarily exclude themselves or to limit their own deposit rates, loss rates, betting rates, or periods of play.

¹⁶ Noted in an August 4, 2009 interview with Simon Holliday, Director of H2 Gambling Capital (U.K.).

¹⁷ Franklin (2001) discusses lack of federal funding for treatment or awareness of problem gambling, lack of insurance parity for problem gamblers, and limited or lack of funding from most states in the United States. Joanna Franklin, *Problem Gambling in the U.S: From the Beginning – Into 2001*, http://www.responsiblegambling.org/articles/Problem_and_Pathological_Gambling_A_view_from_the_States.pdf (last accessed on September 10, 2009). Also, Winslow (2008) discusses the lack of state funding for problem gambling services in Colorado and other states in the United States. Kyle Winslow, "A Problem for Gamblers," *The American Prospect*, March 10, 2008, http://www.prospect.org/cs/articles?article=a_problem_for_gamblers (last accessed on July 13, 2009). Also see the website of the Association of Problem Gambling Service Administrators (APGSA), <http://www.apgsa.org/State/index.aspx> (last accessed on September 10, 2009).

We believe that the opportunities to mitigate problem gambling provide significant benefits not available under the status quo. These benefits provide a significant counterweight to any potential increases in problem gambling that result from legalization. Furthermore, the potential benefits of mitigation would become available to most existing online problem gamblers.\

E. Conclusions

We have examined 10 distinct risks in four categories that may be associated with the growth and availability of online gambling. In each case, the current legislative framework is failing to provide any effective risk control or consumer protection. The establishment of a well-regulated industry under U.S. jurisdiction would offer the opportunity for much better protection. We recommend that plans for regulating online gambling include the design and use of different risk-control strategies for different risks that may be associated with Internet gambling, as well as education and consumer support.

If the United States decides to legalize and regulate online gambling sites, we would expect most U.S.-resident gamblers to be diverted from overseas sites toward reputable and trusted domestic operators. In the long run, reputable gambling operations under U.S. control should come to dominate online gambling opportunities chosen by U.S. consumers. All four categories of risk would be better controlled in such circumstances than they are at present. In the end, U.S. consumers would be better protected than they are now.

II. REGULATORY METHODS AND TECHNOLOGIES AVAILABLE FOR CONTROLLING EACH RISK

For each of the 10 risks outlined above, a set of regulatory methods and technologies already exists that would provide a reasonable degree of control. Moreover, most of them have been implemented successfully in other countries and other online settings. This section describes a variety of control technologies and regulatory tactics relevant to each risk, and identifies the most promising approaches in each case.

A. Gambling by Minors

A common concern about legalizing online gambling stems from the fact that many current online gambling sites do not have adequate regulations or safeguards against gambling by minors. The primary concern is that underage access to and use of online gambling services might increase because it may be difficult to verify age and replicate controls used by bricks-and-mortar casinos to exclude minors. However, effective measures to prevent online gambling by minors have been implemented in well-regulated Internet gambling environments in many European countries and in Australia. Moreover, a number of technologies routinely used in other industries can be applied to the online gambling environment. We discuss below the issue of online gambling by minors and strategies to prevent it.

1. The Issue of Gambling by Minors

Age restrictions apply to virtually all forms of legalized gambling, though the specific age restriction varies by jurisdiction. The typical rationale for age restrictions is that children and young persons are highly vulnerable and are more likely to become problem gamblers if they begin gambling at a young age. In the online environment, gambling by minors is a problem that stems from the inherent difficulty in separating underage users from adults on the Internet because of the absence of an official personally verifying a gambler's age.¹⁸ Minors can gain access to online gambling websites either by providing false credentials during the registration process or by gaining access to their parents' or others' online gambling account.

Anecdotal evidence suggests and surveys have shown that underage gambling is widespread. Studies conducted between 1999 and 2004 covering Canada, the United States, the United Kingdom, and Australia indicated that 4–7% of adolescents exhibited serious patterns of pathological gambling and 10–15% were at risk of either developing or returning to a serious gambling problem.¹⁹ More recent studies have revealed an increase in the involvement of

¹⁸ Ryan S. Landes, "Layovers and Cargo Ships: The Prohibition of Internet Gambling and a Proposed System of Regulation," *New York University Law Review*, 82 (May 2007): 913–943 at p. 923.

¹⁹ Sally Monaghan, *Internet and Wireless Gambling – A Current Profile*, Australasian Gaming Council, 2008. http://www.austgamingcouncil.org.au/images/pdf/Discussion_Papers/agc_dis_internet.pdf (last accessed on July 11, 2009). Also the extent to which rates of problem gambling among adolescents are elevated is controversial. For example, in exploring the properties of two screening instruments in identifying problem gambling among students aged 15 to 17, Ladouceur *et al.* (2005) discuss the need to clarify the construct of pathological gambling among youth and note that neither the SOGS nor the DSM-IV subscale (MAGS) was perfect in identifying problem gambling. R Ladouceur *et al.*, "Concordance between the SOGS-RA and the

(continued...)

Canadian youth in online gambling. In 2006, 9% of Canadian high school students reported having gambled online for money, an increase from 3.6% in 2005.²⁰ According to the National Annenberg Survey of Youth, in the United States, card playing for money on the Internet by male youth aged 14 to 22 rose to 3.3% in 2008 from 2.4% in 2007.²¹ In a 2008 study of general gambling attitudes among Canadian youth aged eight to 20, 76% of those surveyed admitted to having gambled at least once in their lives.²² Among the group aged 18 to 20, 90% had gambled at least once and approximately 39% admitted to gambling once a week or more.²³

2. Existing Controls in Other Jurisdictions

States with commercial casino gambling typically limit access to persons 21 or over, although most lotteries and some Native American casinos allow 18-year-olds to gamble. Most other countries have an age limit of 18, which applies to both online and casino gambling. There is no established minimum age for online gambling in the United States because it is done outside of U.S. legal and regulatory safeguards.

Well-regulated overseas gambling jurisdictions require online operators to verify the identity, location, and age of their customers and to use various mechanisms to curb underage gambling. Some evidence suggests that age restrictions for online gambling have not been uniformly required or rigorously implemented. In an exploratory study of 30 U.K.-based sites conducted before the United Kingdom's regulation of online gambling, researchers noted that 11 of those sites had no age verification check.^{24, 25} Although 17 sites had age checks, they simply required a person registering to either check a box to confirm that they were 18 years of age or older or

DSM-IV Criteria for Pathological Gambling among Youth." *Psychology of Addictive Behaviors*, 19, No. 3 (2005): 271-276 at p. 274-275.

²⁰ J. McBride, "Internet Gambling among Youth: A Preliminary Examination," *International Center for Youth Gambling Problems & High-Risk Behaviors Newsletter*, 6, No. 1 (2006); cited in Sally Monaghan, *Internet and Wireless Gambling – A Current Profile*, Australasian Gaming Council, 2008. http://www.austgamingcouncil.org.au/images/pdf/Discussion_Papers/agc_dis_internet.pdf (last accessed July 11, 2009).

²¹ The Annenberg Public Policy Center *Internet Gambling Stays Low Among Youth Ages 14 to 22 but Access to Gambling Sites Continues; Sports Gambling Makes Resurgence*, November 26, 2008, <http://www.annenbergpublicpolicycenter.org/NewsDetails.aspx?myId=306> (last accessed July 25, 2009).

²² Jeffrey L. Derevensky *et al.*, "Adolescent Attitudes toward Gambling," *Brazilian Journal of Cognitive Psychology*, 4, No. 1 (2008), http://pepsic.bvs-psi.org.br/scielo.php?script=sci_arttext&pid=S1808-56872008000100002&lng=en&nrm= (last accessed on September 1, 2009).

²³ See *Id.*

²⁴ U.K.-based online gambling operators first came under regulation with the introduction of the Gambling Act 2005 in September 2007. Before the Gambling Act, online gambling fell under no specific regulation.

²⁵ Michael Smeaton and Mark Griffiths, "Internet Gambling and Social Responsibility: An Exploratory Study," *CyberPsychology & Behavior*, 7, No. 1 (2004): 49-57.

enter their date of birth.²⁶ In addition to lax age checks, most websites required only a valid credit card to begin gambling. However, some minors in the United States as young as 13 have access to credit cards in their name, rendering this mechanism ineffective as an age check.²⁷ Moreover, minors may have access to their parents' credit card information. In a 2004 British study, a 16-year-old girl attempted to access 37 gambling websites using her debit card, lying about her age but being otherwise truthful. Only seven sites prevented her from registering.²⁸

A more recent mystery shopping study performed between April 2008 and March 2009, after U.K.-based online gambling had come under regulation, revealed quite different results. The British Gambling Commission noted that more than 95% of gamblers were registered with websites that had sufficient age verification checks, and only 2.2% were registered with sites that had age verification weaknesses.²⁹

Other jurisdictions have also had success in preventing underage gambling through effective use of restrictions and mechanisms. In his testimony to Congress, the CEO of the Alderney Gambling Commission noted that during the seven years of regulation of online gambling in Alderney, the Commission had not had any complaints about minors gaining access to an Alderney-regulated site. He further noted that the primary reason that Alderney's licensed sites are able to prevent minors from gaining access is the use of third-party verification software by most licensees.³⁰

Similarly, Mary Williams of the Gambling Control Commission of the Isle of Man noted that license holders of online gambling websites use various methods of age verification, including large data services such as Experian, to ensure that customers are of legal age. Moreover,

²⁶ See *Id.*

²⁷ Commission on Child Online Protection, *Report to Congress*, October 20, 2000, <http://www.copacommission.org/report/COPAreport.pdf> (last accessed on August 11, 2009), p. 25. Also see European Commission, *Background Report on Cross Media Rating and Classification, and Age Verification Solutions*, Safer Internet Forum, September 2008, http://ec.europa.eu/information_society/activities/sip/docs/pub_consult_age_rating_sns/reportageverification.pdf (last accessed on August 24, 2009).

²⁸ Smeaton *et al.*, "Study into Underage Access to Online Gambling and Betting Sites," 2004; cited in Ryan S. Landes, "Layovers and Cargo Ships: The Prohibition of Internet Gambling and a Proposed System of Regulation," *New York University Law Review*, 82 (2007), at p. 924.

²⁹ British Gambling Commission, *Online Mystery Shopping Programme*, July 2009, <http://www.gamblingcommission.gov.uk/pdf/online%20mystery%20shopping%20programme%20july%202009.pdf> (last accessed on August 2, 2009).

³⁰ Testimony of André Wilsenach, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 145.

withdrawal of funds requires access to a PIN number, which the gambling site mails to the user's postal address, thereby limiting the possibility of unauthorized access to funds by minors.³¹

Gibraltar's regulatory regime requires licensees to take "all reasonable steps" to verify that customers are of legal age, although operators are allowed to consider the use of a credit card as a verification of age.³²

The United Kingdom requires that licensed gambling sites have policies and procedures to prevent underage gambling, including a warning that underage gambling is illegal, requiring an affirmation from the customer that he or she is of legal age, ensuring that staff are trained in age verification (particularly in the use of secondary forms of identification verified by staff members when initial automated procedures fail), and enabling filtering software to block the website.³³ Beyond this, secondary verification may be required, such as searching credit databases for age information, prohibiting unverified users from withdrawing winnings, and freezing the account of anyone not verified within 72 hours of applying to the site. However, these checks are not required if the user deposits funds using a credit card.³⁴

The regulator in Australia's Northern Territory requires that players' ages be confirmed within 90 days of opening an online gambling account and before withdrawing any funds. Copies of identification must be e-mailed, faxed, or mailed directly to the site operator. If the individual is not confirmed within the 90-day period, he or she must seek permission from the regulator's Director of Licensing to re-open the account.³⁵

In the United States, the UIGEA exempts certain forms of gambling, such as horse racing and state lotteries, from its criminal provisions if the applicable state law has a provision for age verification that is "reasonably designed to block access to minors."³⁶

³¹ Testimony of Mary Williams, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 130.

³² Gibraltar Regulatory Authority, *Code of Practice for the Gambling Industry*, Issued by the Gambling Commissioner, December 13, 2008, http://www.gra.gi/sites/gambling/downloads/215/generic_code_v1.0.2009.pdf (last accessed on August 6, 2009), p. 14.

³³ British Gambling Commission, *Conditions and Codes of Practice applicable to: Remote Casino Licenses, Remote Casino Ancillary Licenses*, December 2008, at p. 7-8.

³⁴ See *Id.*

³⁵ Noted in an August 31, 2009 correspondence with John Sealy, Manager of Information Systems and Technology Services at the Licensing, Regulation and Alcohol Strategy division of the Northern Territory Department of Justice (Australia).

³⁶ Anthony Cabot and John Aristotle Phillips, "Age Verification: UIGEA Compliance and Regulation," *World Online Gambling Law Report*, October 2006, <http://integrity.aristotle.com/documents/AgeVerificationLawPublication.pdf> (last accessed on August 10, 2009).

3. Relevant Technologies for Risk Mitigation

Although the anonymous nature of online platforms might increase the risk of underage gambling, available technologies can address such risks.

Researchers have outlined several categories of technologies for verifying the age of adults, including comparison of the registrant's credentials against public databases such as credit reports and criminal histories, or even biometrics.³⁷ In designing such controls, care would be needed to balance the (intended) exclusion of minors against the (unintended) denial of admission to qualified adults. The use of a credit card can often be an indicator of age, although, as noted in Section 2, some children have access to credit cards, and credit card companies do not allow cards to be used for age verification.³⁸ It is thus likely that any age verification technology would use government-issued identification as its basis, potentially combined with other strategies to increase its effectiveness.³⁹

Exclusion of minors from online gambling can also be aided through technologies routinely used to verify age in other applications today.⁴⁰ Currently, online liquor stores employ various mechanisms, including a variety of data-matching techniques, to prevent minors from purchasing alcohol online.⁴¹ The simplest solution requires a social security number and other forms of identification such as a driver's license, combined with a credit card registered to that individual.⁴² An age-verification service is used to check the information provided against a database containing credit data, driver's license data, and registered voter information.⁴³

³⁷ Internet Safety Technical Task Force, *Enhancing Child Safety and Online Technologies*, Final Report to the Multi-State Working Group on Social Networking of State Attorneys, Berkman Center for Internet & Society, Harvard University, December 31, 2008, http://cyber.law.harvard.edu/sites/cyber.law.harvard.edu/files/ISTTF_Final_Report.pdf (last accessed on September 11, 2009) at p. 8.

³⁸ See *Supra* at footnote 36.

³⁹ See *Id.*

⁴⁰ Such as online liquor stores, online sellers of tobacco, and the websites of Hollywood movie studios. See Testimony of Michael Colopy, in U.S. House of Representatives, Committee on the Judiciary, *Establishing Consistent Enforcement Policies in the Context of Online Wagers*, 110th Cong., 1st Session, November 14, 2007, at p. 53.

⁴¹ Boris Reznikov, "Can I See Some ID? Age Verification Requirements for the Online Liquor Store," *Shidler Journal for Law, Commerce & Technology* 4, No. 5 (2007), <http://www.lctjournal.washington.edu/Vol4/a05Reznikov.html> (last accessed on July 25, 2009). Also see Integrity, *Case Study: Age Verification for Online Alcohol Sales*, Aristotle Inc., http://integrity.aristotle.com/documents/Online_Wine_Sales-WhitePaper2006.pdf (last accessed on September 10, 2009).

⁴² See *Id.*

⁴³ Noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority.

Aristotle, Inc., a technology consulting firm, produces an identity- and age-verification service called Integrity:Direct, which uses a database of government-issued identification to verify age; the vendor claims the check takes less than 5 seconds, covers 3.4 billion people, complies with U.S. privacy laws, and is not subject to the Fair Credit Reporting Act because it does not use any credit data.⁴⁴

LexisNexis and its advanced linking technology combines real time access to billions of public records compiled from thousands of public and proprietary sources that can be used to verify age and identity of individuals.⁴⁵ For a minor to defeat this method of authentication, he or she would have to access an adult's government-issued ID card, credit card, and other information. Because this is a foreseeable scenario, this age verification technique must be combined with others.

Michigan's Liquor Control Commission has approved a "knowledge based authentication" tool for age verification. This online tool develops questions that only the specific individual would know answers to and checks the answers against public records.⁴⁶ This system, while robust, imposes potentially significant transaction costs of between 25 cents and one dollar per check, making it a costly solution if used every time a user logs on to a gambling site.⁴⁷ The LexisNexis service can deliver an interactive, knowledge-based query process to instantly "multifactor" authenticate individuals at the point of customer contact.⁴⁸

Other technologies may prove useful to augment traditional verification, such as the use of a PIN number mailed to the address of record of the user, as in the Isle of Man, or requiring the user to enter personal information via his or her home phone. This strategy prevents a minor from simply using his or her parents' credit and ID cards and immediately creating an account.

If legalization is implemented and matching techniques are used, the U.S.-licensed site operators would be expected to develop and use filters that are discriminating. Regulators could choose where to set the balance between Type I errors (where underage gamblers are not detected) and Type II errors (where gamblers of legal age are excluded). Moreover, with respect to U.S.

⁴⁴ Integrity, *Integrity:Direct*, Aristotle Inc., http://integrity.aristotle.com/index2.php?option=com_content&do_pdf=1&id=47 (last accessed on August 11, 2009).

⁴⁵ Noted in an August 10, 2009 interview with Chris Pinion, National Account Manager at LexisNexis Risk and Information Analytics.

⁴⁶ See *Supra* at footnote 41. Also see Tricia Pearson, 'Can I See Some ID?' *Why Age Verification Is a Hot Topic for Online Retailers*, Shoosmiths, June 24, 2009, <http://www.shoosmiths.co.uk/news/2372.asp> (last accessed on August 11, 2009).

⁴⁷ See *Supra* at footnote 41 Boris Reznikov.

⁴⁸ Noted in an August 10, 2009 interview with Chris Pinion, National Account Manager at LexisNexis Risk and Information Analytics.

residents, we would expect available data to be of high quality and reliability, making age verification through matching techniques effective.⁴⁹

Site operators could also be required to provide child-protective software to parents to keep minors from accessing their parents' accounts or any online gambling sites. The Nova Scotia Gaming Corporation (NSGC) commissioned and distributed BetStopper, which is a software program designed to help parents prevent children from visiting online gambling websites. Results from the pilot survey were extremely positive and indicated that 92% of parents found BetStopper to be a valuable prevention tool.⁵⁰ The BetStopper software was provided to families for free by the NSGC. Other widely available Web filtering software, such as Net Nanny, can also be used to block access to gambling sites by children. Net Nanny analyzes keywords and objects on every website visited and assigns "points" in different content categories, one of which is gambling.⁵¹ If a site scores too high in an objectionable category, the software blocks it.⁵² An administrator, usually a parent, can decide which categories to block and also whether a particular score leads simply to a warning message or to a complete block.⁵³ The software has generally received high reviews, and its filtering technology is resistant to circumvention.⁵⁴ Other parental control tools are contained within operating systems such as Windows Vista and Mac OS X, some are provided for free by network service providers, and many online safety organizations provide directories to help parents find appropriate protective software.⁵⁵ A regulator may require that approved filtering software be offered to anyone requesting it.

Minors may also have a weak financial motive to gamble online. If a minor usurps an adult's payment and identification information, for example, all of the minor's winnings would be paid

⁴⁹ Noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority. Also noted in an August 21, 2009 interview with Andrew Fritchie, General Counsel of PartyGaming PLC.

⁵⁰ Nova Scotia Gaming Corporation, World-Leading Software Launched to Protect Nova Scotia Youth, May 29, 2009, <http://www.nsgc.ca/pdf/press/Microsoft%20Word%20%20BetStopper%20Media%20Release%20FINALMay%2028%20w%20photo.pdf> (last accessed on September 10, 2009).

⁵¹ Net Nanny, Protecting Your Family on the Internet, white paper, http://www.netnanny.com/products/netnanny/protecting_your_family (last accessed on September 10, 2009).

⁵² See *Id.*

⁵³ See *Id.*

⁵⁴ For a review of the Net Nanny software, see <http://internet-filter-review.toptenreviews.com/netnanny-review-pg2.html> (last accessed on September 10, 2009).

⁵⁵ Federal Communications Commission, Report in the Matter of Implementation of the Child Safe Viewing Act; Examination of Parental Control Technologies for Video or Audio Programming, MB Docket No. 09-26, released August 31, 2009, at ¶142, http://hraunfoss.fcc.gov/edocs_public/attachmatch/FCC-09-69A1.pdf (last accessed on September 1, 2009).

directly to the adult's account.⁵⁶ For a minor to benefit financially from gambling, he or she would have to have access to his or her own payment mechanism, such as a credit card or bank account, but the demographic information associated with the account would more easily allow the website to verify the user's age. Similarly, the regulator could require forfeiture to the government of winnings to gamblers who are discovered to be underage, further lowering the financial incentive for minors to gamble online.⁵⁷

Regulators could impose harsh penalties on site operators with lax mechanisms to prevent underage gambling. Frequent and widespread mystery shopping, as done in the United Kingdom, can reveal operators with inadequate safeguards in place to curb underage gambling. The regulator can impose penalties on such operators, including monetary fines, the revocation of the gambling license, and even criminal liability.

Moreover, to help combat underage gambling, a portion of online gambling tax revenues could be earmarked for educational programs for parents and minors. Given sufficient funds, a regulator may require that youth gambling prevention lessons be incorporated into school curricula. In South Australia, the "Don't Bet On It!" program was introduced as a way to educate children about the dangers of youth gambling. A 2002 report claimed a "small but statistically significant change in student attitudes towards gambling" as a result of the curriculum, which includes five lessons, a mock gambling game, and pre- and postactivity surveys.⁵⁸ The report also describes other educational programs from entities in Australia and in North America, such as the Minnesota Institute of Public Health and Saskatchewan Health in Canada.⁵⁹

4. Conclusion

The current state of affairs, with U.S. residents accessing online gambling sites with widely varying degrees of regulation, does not provide comprehensive protections to ensure that gamblers are of legal age. Regulatory mechanisms and technological solutions, many of which are currently used in other jurisdictions and industries, can equip online gambling operators with capabilities to selectively exclude minors from engaging in online gambling. Age verification policies would be less effective in the absence of support from minors' parents and guardians; therefore, a successful regulatory strategy would provide tools with which parents can limit

⁵⁶ Jonathan Gottfried, "The Federal Framework for Internet Gambling," *Richmond Journal of Law & Technology*, X, No. 3, at p. 10, <http://law.richmond.edu/jolt/v10i3/article26.pdf> (last accessed on August 6, 2009).

⁵⁷ Noted in an August 5, 2009 interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia).

⁵⁸ Loris Glass, *Gambling Education: Some Strategies for South Australian Schools*, funded by the Gamblers Rehabilitation Fund, South Australia, November 2002, at p. 19-20, <https://www.library.health.sa.gov.au/Portals/0/gambling-education-some-strategies-for-south-australian-schools.pdf> (last accessed on September 10, 2009).

⁵⁹ See *Id.* at p. 20-22.

access to gambling websites by their children. We believe that online gambling can effectively exclude minors when it combines cutting-edge technology with a strong regulatory regime.

B. Defrauding of Consumers by Site Operators

Gambling websites, which deal with large amounts of money in a virtual setting, have the potential for fraudulent activity and unfair dealings.⁶⁰ As discussed below, unregulated gambling sites have been known to defraud customers and steal significant sums of money.⁶¹ However, a system of effective regulation could manage the risks of fraud and ensure fair and legal dealings.

1. The Issue of Fraud by Site Operators

Fraud by site operators can be classified into three broad categories:

- Individuals can set up unlicensed gambling websites that either refuse to return customers' deposits or operate unfair games.
- Operators can model a fraudulent website after a licensed site and siphon players from the more reputable operator.
- Insiders within reputable websites can exploit inside information to cheat players without the knowledge of the larger organization.

It is reasonably easy for an individual to set up a fraudulent site, attract as many depositors as possible, and then either shut down the site and take the deposits or continue to run the site with odds or fees swung decidedly in the operator's favor. As a site's reputation became tarnished, it would quickly lose its base of players, but it could then simply shut down and open a new site, perpetrating the same fraud over and over again.⁶² The identity of site owners is often unclear, and the ease of transferring between sites makes this method of fraud highly profitable.⁶³

Reputation is clearly a major attribute of gambling websites. Websites can piggyback on, or usurp, the reputation of a reputable operator or jurisdiction to instill confidence in consumers. For instance, "Casino Australia (<http://www.casinoaustralia.com/>) is an attractive site emblazoned with images of Sydney, koalas, and the national flag but has no other connection with Australia. The online casino is physically located in the Netherlands Antilles and marketed

⁶⁰ Gerd Alexander, "The U.S. on Tilt: Why the Unlawful Internet Gambling Enforcement Act is a Bad Bet," *Duke Law & Technology Review*, 5 (2008), at ¶9.

⁶¹ See, for example, Financial Crimes Enforcement Network, *A Survey of Electronic Cash, Electronic Banking, and Internet Gaming*, U.S. Department of the Treasury, 2000, at p. 41; and see *Supra* at footnote 18 at p. 925.

⁶² See *Supra* at footnote 18, at page 925.

⁶³ See *Id.*

by a Native American gambling corporation.”⁶⁴ Because gambling websites are often based in countries far from their target customers, they can often avoid legal accountability, and because website creation is relatively simple, a customer can be easily confused about the licenses and controls held by a particular site.⁶⁵

In addition to fraud by gambling sites themselves, employees or executives of sites may initiate fraud at the individual level without the knowledge of the organization as a whole. In September 2007, players at the poker website Absolute Poker initiated their own investigation into apparent cheating by a player in a tournament. The investigation revealed that a co-owner of the company and a former director of operations had acted in concert to cheat players of amounts between \$500,000 and \$1 million.⁶⁶ Another poker website, UltimateBet, was rocked by a cheating scandal in early 2008 triggered by concerns about one online player who could apparently see other players’ hole cards during play. Investigation revealed that from January 2005 to December 2007, former employees of the company, operating from outside, had exploited security vulnerabilities in the site’s software of which only they were aware.⁶⁷

Since the enactment of the UIGEA, U.S. residents no longer have access to large gambling sites operated by publicly-traded companies; instead, U.S. gamblers look to less transparent offshore site operators that may be more likely to engage in fraud or other deceitful practices.⁶⁸ Also, given the current absence of regulatory oversight in the United States, U.S. gamblers have little or no recourse to authorities when site operators defraud them.⁶⁹

The extent of fraud by site operators is not well documented, but cases have been recorded. A 2000 report by the Financial Crimes Enforcement Network of the U.S. Department of the Treasury claims that “[t]here is, in fact, a substantial record of shadow websites collecting...deposits for a period of time and then disappearing, in the process destroying

⁶⁴ Roger Clarke and Gillian Dempsey, “The Feasibility of Regulating Gambling on the Internet,” *Managerial and Decision Economics*, 22 (2001): 125–132, at p. 128.

⁶⁵ See *Id.*

⁶⁶ Russell Goldman, “Online Poker Players Expose Alleged Fraud,” *ABC News*, October 19, 2007. <http://abcnews.go.com/print?id=3752500> (last accessed on July 24, 2009)

⁶⁷ UltimateBet.com, *UltimateBet Issues Statement Regarding Unfair Play*, May 29, 2008. <http://www.ultimatebet.com/poker-news/2008/may/NioNio-Findings> (last accessed on July 24, 2009). Also see UltimateBet.com, *Status Update on NioNio Investigation*, July 8, 2008, <http://www.ultimatebet.com/poker-news/2008/july/Investigation-Status-Update> (last accessed on July 24, 2009).

⁶⁸ As noted in an August 21, 2009 interview with Andrew Fritchie, General Counsel of PartyGaming PLC, U.S. customers are forced to use privately-held sites, which are generally perceived as less reputable.

⁶⁹ See *Supra* at footnote 18 at p. 926. Also see *Supra* at footnote 60 at ¶¶14–15. Also see Christopher Grohman, “Reconsidering Regulation: A Historical View of the Legality of Internet Poker and Discussion of the Internet Gambling Ban of 2006,” *Journal of Legal Technology Risk Management*, 1, No. 1 (Fall 2006): 34–74, at p. 62–63.

consumer confidence.”⁷⁰ In a 2006 survey, the American Gaming Association reported that 55% of respondents “agree[d] at least somewhat that online casinos find ways to cheat players.”⁷¹ The website *GamesandCasino.com* maintains and publishes a long “blacklist” of websites that cheat, defraud, or otherwise manipulate their users.⁷² Finally, in a 2007 survey of Nevadans conducted by the International Gaming Institute at the University of Nevada, Las Vegas (UNLV), 66.9% of respondents (who were not necessarily gamblers) claimed to have “strong doubts about the integrity of online gambling as it pertain[s] to the ability to cheat the gambler.”⁷³ The survey also includes various anecdotes from respondents about cheating by site operators.⁷⁴

In addition to outright fraud by site operators, operators may become bankrupt or otherwise insolvent without engaging in questionable business practices. Without adequate financial protection, customers could lose their entire fund balance with the site.⁷⁵ As shown below, existing controls such as holding customers’ funds in a trust account or establishing financial reserves can help mitigate against this business risk to customers.

2. Existing Controls in Other Jurisdictions

Most regulatory regimes address the issue of operator fraud. In the United States, a regulatory strategy could combine elements from other regimes and add unique safeguards. Below are descriptions of approaches taken to prevent operator fraud in other jurisdictions:

- The Gambling Control Commission of Alderney, a Channel Island, requires sites to have “provisions enabling the customer to address complaints and disputes to an independent body.”⁷⁶
- In the Isle of Man, site operators are required to maintain either financial reserves or a bond to ensure that players are paid their winnings.⁷⁷

⁷⁰ Financial Crimes Enforcement Network, *A Survey of Electronic Cash, Electronic Banking, and Internet Gaming*, U.S. Department of the Treasury, 2000, at p. 41.

⁷¹ American Gaming Association, *State of the States: The AGA Survey of Casino Entertainment*, 2006, at p. 21, http://www.americangaming.org/assets/files/2006_Survey_for_Web.pdf (last accessed on July 23, 2009)

⁷² GamesandCasino.com, *Blacklisted Casinos*, <http://www.gamesandcasino.com/blacklist.htm> (last accessed on September 10, 2009).

⁷³ See *Supra* at footnote 6 Bo Bernhard at p. 37–38.

⁷⁴ See *Id.* at p. 40–43.

⁷⁵ Noted in an August 27, 2009 interview with André Wilsenach, Chief Executive Officer of the Alderney Gambling Control Commission.

⁷⁶ See *Supra* at footnote 30 at p. 142–143.

⁷⁷ See *Supra* at footnote 31 at p. 124.

- Antigua's and Barbuda's regulations require a site operator to maintain "investments that have a market value...of not less than the aggregate amount of all its outstanding prizes and monies held on account for players."⁷⁸
- The British Gambling Commission sets forth rules governing licensed gambling website operators, including one that requires that licensees (1) inform customers as to whether their funds are protected in the event of insolvency and (2) "be able to provide evidence to the [U.K. Gambling] Commission, if required, showing how they satisfied themselves that their terms are not unfair."⁷⁹ The U.K. Department of Culture, Media and Sport (the sponsor of the Gambling Commission) publishes the "White List," a list of nations hosting online gambling whose licensees are legally permitted to advertise in the U.K, although the list is currently in a state of suspension.⁸⁰
- Tasmania's regulator sets technical standards and uses independent accredited testers to verify compliance before approving new software, and for some types of operations also requires that players funds be held in a trust for the protection of players.⁸¹
- Gibraltar's regulator requires licensees to have strong internal controls and also requires independent testing of gambling software to ensure integrity.⁸²

Although the regulatory schemes described above include provisions to prevent fraud, effective regulation must include strong penalties for noncompliance and safeguards that protect customers in the event of fraud or wrongdoing. They also should mandate ordinary but rigorous due diligence by regulators and owners, including background checks on owners, operators, and

⁷⁸ Antigua and Barbuda – Directorate of Offshore Gaming, "Interactive Gaming and Interactive Wagering Regulations," at §184(a).
http://www.antiguagaming.gov.ag/files/Antigua_and_Barbuda_Gaming_Regulations-Final.pdf
 (last accessed July 23, 2009)

⁷⁹ See *Supra* at footnote 33 at p. 14.

⁸⁰ Jamie Wiebe *et al.*, *Problem Gambling Prevalence Research: A Critical Overview*, report to the Canadian Gaming Association, December 2007, at p. 17,
http://canadiangamingassociation.com/media_uploads/pdf/78.pdf
 (last accessed on July 11, 2009). Also noted in interviews with Matthew Hill, Director of Strategy, Research and Analysis at the British Gambling Commission, Paul Morris, Policy Development Manager at the British Gambling Commission, and Peter Collins, Professor of Public Policy Studies and Director of the Center for the Study of Gambling at the University of Salford (U.K.).

⁸¹ Noted in an August 5, 2009 interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia).

⁸² See *Supra* at footnote 32 at p. 13 and 21.

all staff in key positions. The regulatory regime could also give aggrieved consumers the ability to bring civil lawsuits and other rights of action against the site.

3. Relevant Technologies for Risk Mitigation

An effective regulatory regime must combine strong and competent oversight with an effective method for lodging complaints with the regulator or law enforcement agencies. In the examples of cheating mentioned above, it was only after private investigations by players that the sites themselves and the regulator responded.⁸³ The Kahnawake Gaming Commission, the regulator for both sites noted above, ordered Absolute Poker to institute compliance programs and subject itself to random audits; it also fined the site \$500,000.⁸⁴ Similarly, the Commission ordered UltimateBet to refund any money owed to players who were victims of cheating, modified UltimateBet's control system, and fined the site \$1.5 million.⁸⁵

Another potential risk-mitigating factor within a regulatory regime is the use of *Mutual Recognition Agreements* (MRAs), which are arrangements between nations to recognize each other's regulatory standards and controls in a particular area of commerce.⁸⁶ Much as the United Kingdom's "White List" permits or denies advertising on the basis of the quality of a jurisdiction's regulatory structure, an MRA could be used as a filter for permitted advertising, for referrals between sites, and even as a way of selectively retaining prohibitions on foreign sites on the basis of quality and integrity rather than the simple fact that they are foreign.

Although both monetary sanctions and regulatory oversight are key to effective regulation, technology offers methods to prevent cheating over and above what is available to land- and river-based casinos. PartyGaming Plc is a publicly-traded Internet gambling company regulated in Gibraltar, and its PartyPoker affiliate holds about an 8% share of the world's market for online poker.⁸⁷ PartyGaming's games and its random number generator are tested by iTech Labs, an independent gaming device tester. It is also a member of the European Gaming & Betting Association and of eCOGRA, both of which publish standards for gaming operators.⁸⁸ 888.com,

⁸³ Gilbert M. Gaul, "Players Gamble on Honesty, Security of Internet Betting," *The Washington Post*, November 30, 2008, p. A12.

⁸⁴ Kahnawake Gaming Commission, *In the Matter of Absolute Poker – Investigation regarding Complaints of Cheating*, January 11, 2008. <http://www.kahnawake.com/gamingcommission/KGC-AP-0111.pdf> (last accessed on July 24, 2009), at p. 4.

⁸⁵ Kahnawake Gaming Commission, *Kahnawake Gaming Commission Imposes Sanctions on Ultimate Bet with Regard to Cheating Incidents*, September 29, 2008, <http://www.kahnawake.com/gamingcommission/kgc092908.pdf> (last accessed on July 24, 2009).

⁸⁶ See Public Citizen, *Mutual Recognition Agreements (MRAs)*, <http://www.citizen.org/trade/harmonization/MRA/> (last accessed on August 10, 2009).

⁸⁷ As noted in an August 21, 2009 interview with Andrew Fritchie, General Counsel of PartyGaming Plc. Also see <http://www.partygaming.com/prty/en/ourgames/overview/poker> (last accessed on September 10, 2009).

⁸⁸ See http://www.partypoker.com/about_us/ (last accessed on September 10, 2009).

another publicly traded gambling site based in Gibraltar, also uses iTech Labs for verification and is a member of eCOGRA and the Interactive Gaming Council, an online gambling trade group.⁸⁹ Betfair, an Internet betting exchange based in the United Kingdom, is a member of the Independent Betting Adjudication Service, a third-party adjudicator for gambling disputes.⁹⁰

4. Conclusion

As demonstrated above, the most effective system of regulation to combat site operator fraud combines strict enforcement with cooperation by the site operators themselves. Reputable operators with brands to protect could not afford to risk damage to their reputations, loss of their licenses, or regulatory sanctions. However, this incentive is not perfect, and the regulator must be fully equipped to detect and punish site operator fraud. Regulations may be similar to those that apply in the bricks-and-mortar industry. We expect that the online gambling industry will support a supervisory approach that includes regulatory monitoring and sanctions to help promote and maintain an industry reputation for integrity.

C. Cheating or Defrauding of Players by Other Players

As discussed previously, both Absolute Poker and UltimateBet, two popular online poker websites, were rocked by accusations of cheating in 2007 and 2008.⁹¹ The cheaters were players on the site who had acted in concert with employees of the gambling website. These and other high-profile examples demonstrate the potential for cheating online and the basis for fear among online gamblers of being defrauded by other players. However, a system of regulation promises to rein in such fraudulent activity.

1. The Issue of Players Being Defrauded by Other Players

U.S. gamblers currently lack any effective means to seek remedy from other players for fraud. Because players in the United States engage in online gambling outside of legal and regulatory safeguards, they are unlikely to complain to authorities about cheating experienced on a site: "Individual players are unlikely to volunteer information that would reveal that they have gambled online.... Users who doubt the legality of their own actions are unlikely to snitch."⁹²

Although the extent of player cheating and fraud is not well documented, it is a common concern for online players.⁹³ A 2008 study of Swedish online poker players revealed that one of their

⁸⁹ See <http://www.888.com/> (last accessed on September 10, 2009).

⁹⁰ See <http://content.betfair.com/aboutus/?product=exchange&brand=betfair®ion=GBR&locale=en> (last accessed on September 10, 2009).

⁹¹ See *Supra* at footnote 6 Bo Bernhard.

⁹² See *Supra* at footnote 18 at p. 926.

⁹³ John McMullan and Aunshul Rege, *Cheating and Cybercrimes @ Gambling Sites.com*, presentation to the Alberta Gambling Research Institute Annual Conference, March 2009, slide 2.

biggest concerns was being cheated by other players.⁹⁴ In a 2006 survey, the American Gaming Association reported that 46% of online gamblers believed that other players find ways to cheat.⁹⁵ Finally, the aforementioned 2007 UNLV survey revealed that 63% of respondents were “not at all confident” that other players could not cheat them.⁹⁶ The survey also includes anecdotal evidence from respondents about cheating by players, although evidence on the extent of cheating is generally mixed.⁹⁷

Cheating by players can take various forms:

- *Poker bots* are automated programs that can reportedly play poker at the level of a professional tournament player, using a decision engine utilizing advanced neural network technology.⁹⁸ These bots, such as PokerSmoke, can memorize play styles, recognize betting patterns, and calculate odds, potentially giving those who use them a distinct edge over other players.⁹⁹
- A simpler form of cheating involves *collusion* on online poker tables, in which two or more players work together to share information to gain an unfair advantage over unsuspecting players.¹⁰⁰
- Another form is *multitabling*, in which a person uses multiple accounts to enter a tournament as two or more different players and garners information in a similar way to collusion; this particular type of cheating is clearly not possible in an offline environment.¹⁰¹

⁹⁴ Richard T. A. Wood and Mark D. Griffiths, “Why Swedish People Play Online Poker and Factors that Can Increase or Decrease Trust in Poker Web Sites: A Qualitative Investigation,” *Journal of Gambling Issues*, 21 (July 2008): 80–97 at p. 90.

⁹⁵ See *Supra* at footnote 71.

⁹⁶ See *Supra* at footnote 6 Bo Bernhard at p. 38-39.

⁹⁷ See *Id.* at p. 40–43.

⁹⁸ Mike Brunker, “Poker ‘Bots’ Raking Online Pots?” MSNBC.com, September 21, 2004. <http://www.msnbc.msn.com/id/6002298/print/1/displaymode/1098/> (last accessed on July 25, 2009). Also see *Supra* at footnote 93, slide 7.

⁹⁹ See *Id.*

¹⁰⁰ Bill Rini, The Definitive Guide to Online Poker Cheating, April 16, 2008. <http://www.billrini.com/2008/04/16/the-definitive-guide-to-online-poker-cheating/> (last accessed on July 25, 2009).

¹⁰¹ See *Supra* at footnote 69 Christopher Grohman at p. 63.

- The Absolute Poker and UltimateBet cheating cases, mentioned previously, involved players using “superuser” accounts that allowed them to see other players’ hole cards in online poker, making them essentially unbeatable.¹⁰²
- Hackers can potentially alter sites to ensure winnings or swing odds in their favor, as in a case in 2001 in which hackers rigged games on two gambling sites and managed to win \$1.9 million in just a few hours.¹⁰³

2. Existing Controls in Other Jurisdictions

Although the UltimateBet and Absolute Poker cheating scandals involved participation from insiders at the affected poker sites, it is important to note that both episodes were revealed through the investigative work of other players on the sites.¹⁰⁴ Although players have an incentive to reveal fraud by other players, some level of regulatory oversight and potential law enforcement involvement is needed to ensure that the site operator takes complaints lodged against players seriously. The regulator could mediate disputes between the site operator and players, independently monitor sites for cheating, and work with site operators to help them prevent cheating. The following are examples of ways that other jurisdictions combat player fraud:

- The British Gambling Commission requires that licensees “put into effect a written procedure for handling customer complaints and disputes” and also have arrangements for disputes to be referred to an independent third party if they are not resolved to the customer’s satisfaction.¹⁰⁵
- Tasmania’s Gaming Commission requires that customer complaints can be made to it and has the power to levy fines and revoke sites’ licenses as well as settle customer disputes. It also has access to the systems of its licensees.¹⁰⁶
- Gibraltar also requires that sites have a formal system to handle customer complaints.¹⁰⁷

¹⁰² See *Supra* at footnote 83.

¹⁰³ RSe Consulting, *A Literature Review and Survey of Statistical Sources on Remote Gambling*, October 2006, http://www.culture.gov.uk/images/publications/RemoteGambling_RSeReport.pdf (last accessed on July 25, 2009), at p. 20.

¹⁰⁴ See *Supra* at footnote 66.

¹⁰⁵ See *Supra* at footnote 33 at p. 15.

¹⁰⁶ Noted in an August 5, 2009 interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia).

¹⁰⁷ See *Supra* at footnote 32 at p. 17–18.

- Sites' own terms of service often explicitly preclude certain potentially fraudulent behaviors.¹⁰⁸

3. Relevant Technologies for Risk Mitigation

As with the issue of fraud by site operators, technology offers solutions to help combat fraud by players. The first line of defense is analysis by other players, who may be in a position to observe aberrant behavior, investigate it, and lodge a complaint with the site operator. However, players may have a hard time detecting cheating as it is occurring, because of the speed and style of online gambling. Site operators, on the other hand, can store large volumes of data on gambling transactions and present them in an easy-to-analyze format, unlike operators of land- and river-based casinos. Analysis of hand histories in poker, for example, may allow operators to identify collusion, the use of poker bots, and other unusual gameplay activities.

The regulator may require that the site operator provide these data at regular intervals for analysis in the event that an inquiry or red flag is triggered. It might also mandate implementation of pattern recognition software to scan routinely for anomalous betting patterns. Finally, the regulator could provide sites' data history to third-party verification companies that conduct their own analyses, including checks for randomness, collusion, and other suspicious patterns.

Clearly, players want to know that their online gambling experience is fair. According to the survey of Swedish poker players, "[t]he response of the operator to [issues of cheating] played a major role in whether or not they were trusted in the long term."¹⁰⁹ Gambling sites, especially reputable ones, have an incentive to control cheating to maintain their good reputation. However, although the revelation of cheating can itself be damaging to a site's reputation, the site can often continue to make money as usual even while players are being defrauded.¹¹⁰

A regulatory structure, therefore, must balance these contradictory incentives. It must combine strong internal controls by site operators with strict regulatory oversight, perhaps by requiring that mandatory hand history reports or other similar data be submitted to the regulator or through the use of regulator-verified poker bot detection software.¹¹¹ Also, the regulator could maintain a

¹⁰⁸ For example, multitableting and collusion are considered cheating according to poker room rules. See Christopher Grohman, "Reconsidering Regulation: A Historical View of the Legality of Internet Poker and Discussion of the Internet Gambling Ban of 2006," *Journal of Legal Technology Risk Management*, 1, No. 1 (Fall 2006): 34–74, at p. 63; and Bill Rini, *The Definitive Guide to Online Poker Cheating*, April 16, 2008, <http://www.billrini.com/2008/04/16/the-definitive-guide-to-online-poker-cheating/> (last accessed on July 25, 2009).

¹⁰⁹ See *Supra* at footnote 94 at p. 90.

¹¹⁰ As in the UltimateBet and Absolute Poker scandals. Also see *Supra* at footnote 98 Mike Brunker.

¹¹¹ For example, bwin has dedicated staff that deploy "[s]tate-of-the art systems [that] are used to analyze hands and to detect chip dumping, collusion or the use of poker bots." From an August 13, 2009 correspondence with Katharina Riedl of bwin (Austria).

database of known cheaters, and sites' own verification processes could help exclude such gamblers at the point of registration. This strategy also has the benefit of preventing cheaters from skipping easily from one website to another. Regulation could also grant players the right to bring a civil claim against a gambling site for not preventing cheating by its users, providing additional incentives for sites to implement effective controls.¹¹²

4. Conclusion

Site operators, players, and regulators share an interest in detecting and protecting against player fraud. This naturally leads to cooperative regulatory oversight. Such oversight would recognize the inherent opportunities in the online environment for comprehensive data storage, allowing a level of analysis to detect fraud that is unavailable in the bricks-and-mortar environment. Consequently, legal, regulated online gambling should provide greater protections against player fraud than does the current environment.

D. Involvement of Organized Crime in Gambling Operations

Casino gambling, in which nearly all transactions are in cash, is particularly susceptible to *skimming*, in which profits are removed by the owners or other insiders before being declared, as well as money laundering.¹¹³ Moreover, its illegal status in many jurisdictions implies that those who offer gambling services in those jurisdictions are, by definition, law breakers. Online gambling, however, presents different challenges and opportunities than does its bricks-and-mortar counterpart. On the one hand, identities can be easier to conceal online, transactions can occur far from where regulators are located, and members of collaborating crime networks can be located in far-flung locations.¹¹⁴ On the other hand, online transactions are easier to aggregate and analyze, providing richer opportunities to detect the operations of organized crime groups.¹¹⁵ The lack of cash transactions makes auditing and the detection of skimming easier than in a bricks-and-mortar environment.

1. The Issue of Involvement of Organized Crime in Online Gambling

Organized crime has been largely eliminated from bricks-and-mortar casinos.¹¹⁶ In Nevada, for example, the regulatory regime has largely eliminated criminals from the ownership of

¹¹² See *Supra* at footnote 69 at p. 67–68.

¹¹³ Jay Albanese, "Casino Gambling and Organized Crime: More Than Reshuffling the Deck," in *Contemporary Issues in Organized Crime*, edited by Jay Albanese (Monsey, New York: Criminal Justice Press, 1995). Also see Kevin B. Kinnee, *Practical Gambling Investigation Techniques* (New York: Elsevier, 1992), at p. 3–5.

¹¹⁴ See *Supra* at footnote 64 at p. 128.

¹¹⁵ As noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority, online gambling allows a perfect audit trail to be kept.

¹¹⁶ Jay Albanese, "Casino Gambling and Organized Crime: More Than Reshuffling the Deck," in *Contemporary Issues in Organized Crime*, edited by Jay Albanese (Monsey, New York: Criminal Justice Press, 1995), at p. 4–5.

casinos.¹¹⁷ Another factor in the Nevada transformation has been the introduction of large, publicly held companies as casino owners, which cannot afford associations with organized crime.¹¹⁸ The same effect may hold true for online gambling enterprises, some of which are already publicly traded.

In the past, when organized crime had been involved in bricks-and-mortar casinos, it traditionally controlled the gambling organization itself, usually behind the presence of a front man in cases of legal gambling establishments.¹¹⁹ Similarly, gambling websites could be controlled by organized syndicates. Finally, as discussed more fully in Section F, criminals can use online gambling for the purpose of money laundering.

2. Existing Controls in Other Jurisdictions

In bricks-and-mortar casinos, background checks and verification for site operators and employees are standard procedures across all jurisdictions in the United States. In New Jersey, those who wish to operate a casino are required to obtain a casino license.¹²⁰ Applicants must prove their financial stability and integrity; the financial integrity of their investors or backers; their good character, honesty, and integrity; and their business ability and casino experience. They must also submit to a criminal background check.¹²¹ Each casino employee must obtain a valid casino employee license, which involves providing his or her name, address, and fingerprints; and to consent to a criminal background check, which the New Jersey State Police performs at the applicant's expense.¹²² The State Police are also obliged to notify the New Jersey Division of Gaming Enforcement if a license holder is arrested at any point after the initial background check.¹²³ To eliminate small gambling establishments, casinos in Atlantic City are required to have a minimum of 500 hotel rooms, and all games are tightly regulated and controlled. Also, those that provide a certain amount of ancillary services (such as cleaning, food, construction, and security) to casinos must be licensed and submit to background checks.¹²⁴

Similarly, Nevada laws impose on operators of gambling establishments licensing requirements that require that the applicant (1) be a person of good character, honesty, and integrity; (2) be a person whose prior reputation and criminal record do not pose a threat to the public interest of

¹¹⁷ See *Id.* at p. 4.

¹¹⁸ See *Id.* at p. 7-8.

¹¹⁹ See *Id.* at p. 3.

¹²⁰ New Jersey Permanent Statutes, Title 5, Amusements, Public Exhibitions and Meetings, 5:12-82: Casino license – applicant eligibility.

¹²¹ *Id.* at 5:12-84: Casino license – applicant requirements.

¹²² See *Id.*

¹²³ See *Id.*

¹²⁴ See *Supra* at footnote 116 at p. 10.

the state or of its gambling regulations; and (3) have sufficient financial resources and business acumen to operate the establishment.¹²⁵ Employees in general are required to register as gaming employees, to submit fingerprints, and to be subjected to an FBI background check. The Nevada Gaming Control Board is empowered to object to any applicant for “any cause deemed reasonable.”¹²⁶

Many jurisdictions across the world that license online gambling include provisions for checks on the site’s operators. The following are examples of such provisions:

- In the Isle of Man, the Gambling Control Commission has the duty “[t]o investigate the character and financial status of persons behind online gambling operations.”¹²⁷
- The U.K. Gambling Act of 2005 allows the Gambling Commission, when issuing a license, to consider “the integrity of the applicant or of a person relevant to the application” and to refuse a license to a person convicted of a “relevant offence.”¹²⁸
- Alderney’s Gambling Control Commission has the duty to “determine whether an applicant is ‘fit and proper’ to hold a license. Investigations can include interviews with key individuals, and the Commissioners may also require their own meeting with representatives of the applicant before deciding whether to grant a license.”¹²⁹ The regulator also requires that business associates of site operators and software providers hold licenses.¹³⁰
- Tasmania’s Gaming Commission conducts thorough probity investigations on site operators, including credit checks and fingerprint background checks; the checks are also required for employees of the gambling website.¹³¹

¹²⁵ Nevada Revised Statutes, Chapter 463.170.

¹²⁶ *Id.* at Chapter 463.335.

¹²⁷ See *Supra* at footnote 31 at p. 128.

¹²⁸ Gambling Act, 2005 Chapter 19 (Eng.), at §§70–71, http://www.opsi.gov.uk/acts/acts2005/pdf/ukpga_20050019_en.pdf (last accessed on September 11, 2009).

¹²⁹ See *Supra* at footnote 30 at p. 140–141.

¹³⁰ Noted in an August 27, 2009 interview with André Wilsenach, Chief Executive Officer of the Alderney Gambling Control Commission.

¹³¹ As noted in an August 5, 2009 interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia).

- The regulator in Australia's Northern Territory checks the reputation of operators and their associates and proposed managers, as well as operators' financial background, resources, and business ability.¹³²
- Gibraltar's Gambling Act 2005 prevents the licensing authority from granting a license to a person who is not "fit and proper" or if granting the license would be against the public interest. The Gambling Act allows the regulator to take into account the licensee's character, honesty, and integrity, as well as his or her reputation, business plan, experience, and other factors.¹³³

As can be seen, each jurisdiction considers the exclusion of criminals to be essential to maintaining an effective regulatory regime.

3. Relevant Technologies for Risk Mitigation

Any regulatory regime that wishes to exclude criminals must focus on erecting sufficiently high barriers to entry.¹³⁴ Simple techniques such as requiring background checks, interviews, and letters of reference can familiarize the regulator with its license applicants and allow it to make a more informed decision on whether to grant a license. This level of investigation of site operators could extend to owners, beneficiaries, business associates, managers, and security personnel.¹³⁵ Rigorous vetting of new applicants can combine with ongoing compliance checks to ensure that once a license is granted, it is not clandestinely transferred to criminal control.

4. Conclusion

Although criminal control of gambling websites is a possibility, strict regulation would exclude unwanted site operators. It is unlikely that criminals would subject themselves to strict regulatory checks and demanding admission standards. Instead, they may attempt to operate gambling sites without licenses. Regulators can work to educate consumers about the dangers associated with unlicensed websites, and steer them toward licensed, regulated sites which offer protection against criminal activity. At the risk of losing their licenses, legitimate operators would have a strong interest in avoiding ineligible associates as is the case with bricks-and-mortar casinos. We would expect legitimate, licensed sites to be receptive to a fair degree of scrutiny because such scrutiny would enhance the reputation of the industry.

¹³² As noted in an August 31, 2009, correspondence with John Sealy, Manager of Information Systems and Technology Services at the Licensing, Regulation and Alcohol Strategy division of the Northern Territory Department of Justice (Australia).

¹³³ Gibraltar Gambling Act 2005, Schedule 1, at §3, <http://www.gra.gi/sites/gambling/downloads/42/gambling%20ord%202005.pdf> (last accessed on August 6, 2009).

¹³⁴ See *Supra* at footnote 30 at p. 140.

¹³⁵ See *Id.*

E. Money Laundering by Players

A major concern of law-enforcement authorities is money laundering facilitated by online gambling.¹³⁶ However, many financial analysts believe that the risks of money laundering in online gambling is low because electronic transactions are closely monitored and recorded.¹³⁷ A combination of anti-money-laundering regulations, currently in place for bricks-and-mortar casinos as well as other financial institutions, and the use of technology would provide the online gambling environment with better opportunities for detecting money laundering by players than those available in land- and river-based casinos.

1. The Issue of Money Laundering by Players

Money laundering is a process through which proceeds derived from illegal activity are legitimized.¹³⁸ Money laundering is typically accomplished in three stages: (1) the placement stage, (2) the layering stage, and (3) the integration stage.¹³⁹ The *placement* stage is defined as the first entry of illegal money into financial institutions or the retail economy. The *layering* stage consists of activities meant to hide the trail of money, generally involving the transfer of money among multiple entities. The final stage, the *integration* stage, is when the illegal funds are reintroduced into the economy to appear as though they were legitimate. It is difficult for law enforcement to detect this reintroduction of illicit funds into the economy without an audit trail established during the first two stages of the laundering process.¹⁴⁰

The following (hypothetical) example demonstrates how online gambling websites can be used to launder money: A customer could establish an Internet gambling account under a false name and use illicit funds to conduct a minimal amount of betting. After a few losses, the customer could request repayment from the Internet gambling site and claim them as winnings, thereby creating a legitimate source for the remaining funds.¹⁴¹

The U.S. Department of Justice is concerned that online gambling offers criminals an easy vehicle for money laundering because of its anonymous nature, use of encryption, volume,

¹³⁶ Government Accountability Office, *Internet Gambling: An Overview of the Issues*, GAO-03-89, December 2002, at p. 34-37.

¹³⁷ See *Id.* at p. 37-38.

¹³⁸ Mark D. Schopper, "Internet Gambling, Electronic Cash & Money Laundering: The Unintended Consequences of a Monetary Control Scheme," *Chapman Law Review*, 5, No. 1 (2002): 303-330.

¹³⁹ Financial Crimes Enforcement Network, *The SAR Activity Review – Trends, Tips & Issues*, May 13, 2008, http://www.fincen.gov/news_room/rp/files/sar_tti_13.pdf (last accessed on August 5, 2009).

¹⁴⁰ See *Supra* at footnote 138.

¹⁴¹ Testimony of John G. Malcolm Before the Committee on Banking, Housing, and Urban Affairs, March 18, 2003, <http://www.usdoj.gov/criminal/cybercrime/malcolmTestimony318.htm> (last accessed on September 11, 2009). Also see *Supra* at footnote 136.

speed, international reach, and offshore locations.¹⁴² In his testimony before Congress in 2003, Deputy Assistant Attorney General John G. Malcolm noted that e-casinos are an excellent vehicle for money laundering because in addition to using the gambling services offered to hide or transfer money, online gambling websites offer a wide variety of financial services to their customers, including credit accounts, fund transmittal services, check cashing services, and currency exchange services.¹⁴³

There is little documentation by which to gauge the extent of actual money laundering in online gambling. In 2002, the U.S. General Accounting Office (GAO) examined the vulnerability of online gambling to money laundering and concluded that the "views on the vulnerability of Internet gambling to money laundering are mixed."¹⁴⁴ Its report provides only hypothetical examples of how online gambling sites could be used to launder money and does not describe any actual cases. A 2005 report prepared for the Interactive Gaming Council in Canada calls evidence of the existence of money laundering in online gambling "scant" and claims that the Internet Crime Complaint Center had never logged a complaint of money laundering through gambling sites.¹⁴⁵ It goes on to claim that "Internet gaming does not, in and of itself, contribute to money laundering. Rather, it is the financial transactions that are used to move money on the Internet that may be susceptible to money laundering."¹⁴⁶

One can understand money laundering patterns that might occur in online gambling by extrapolating from the patterns of money laundering seen in bricks-and-mortar casinos. Various betting patterns associated with money laundering in bricks-and-mortar casinos have been identified, including the use of hedged bets by colluding players, light betting or *minimal play* (i.e., using bets that are small relative to the size of deposits and withdrawals), splitting transactions up into units smaller than reporting thresholds, splitting transactions across reporting "days," and pressuring staff to not comply with their reporting obligations.¹⁴⁷

A problem related to money laundering is that of terrorist financing, in which funds that are intended for terrorist groups are moved through the financial system in an apparently legitimate way. Effective anti-money-laundering provisions must specifically address the risks of terrorist financing, although many techniques to combat money laundering are also effective against

¹⁴² See *Id.* John G. Malcolm.

¹⁴³ See *Id.*

¹⁴⁴ See *Id.*

¹⁴⁵ NFC Global, "Internet Gaming & Money Laundering: Measuring the Scope, Assessing the Risks," Prepared for the Interactive Gaming Council, Vancouver, British Columbia, Canada, August 2005, at p. 4.

¹⁴⁶ See *Id.*

¹⁴⁷ American Gaming Association, Suspicious Activity Reporting Policy, [http://www.americangaming.org/assets/files/SARC_Policy_\(6\).pdf](http://www.americangaming.org/assets/files/SARC_Policy_(6).pdf) (last accessed on July 28, 2009).

terrorist financing.¹⁴⁸ The only known case of money laundering through gambling sites was related to terrorist financing: in 2007, a suspected terrorist named Al-Daour used stolen credit cards to deposit funds at 43 different gambling sites and then withdrew the winnings to various online bank accounts.¹⁴⁹

2. Existing Controls in Other Jurisdictions

Congress has enacted legislation to detect money laundering. Under the Bank Secrecy Act (BSA) of 1970, all U.S. financial institutions, including banks, credit unions, securities firms, and casinos, are required to report large currency transactions and suspicious activities.¹⁵⁰ The Financial Crimes Enforcement Network (FinCEN) administers these regulations. The casino gambling industry has been covered by the BSA since 1985, and FinCEN has specific regulations that pertain to casino gaming. The BSA requires the reporting of any currency transactions exceeding \$10,000 in a single gaming day on a Currency Transaction Report (CTR).

¹⁵¹ Because money launderers can structure transactions such that they never result in a CTR being filed, all land- and river-based casinos are also required to file Suspicious Activity Reports (SARs). Casinos have to file SARs if they know, suspect, or have reason to suspect that a transaction involving \$5,000 or more meets certain criteria, including involvement of illicit funds, intention to avoid or prevent proper reporting, exhibiting of abnormal behavior, or use of the casino to facilitate criminal activity.¹⁵²

The leading online gambling jurisdictions have created regulatory structures that resemble traditional regulation for land- and river-based casinos in the United States. These jurisdictions require some form of anti-money-laundering monitoring, ranging from restricting customers to a single account to identifying and reporting suspicious transactions or players' abnormal betting patterns.¹⁵³

In addition to regulation that combats money laundering in its financial services sector, the Isle of Man has put in place the Anti-Money Laundering Code to prevent money laundering through gambling websites.¹⁵⁴ Operators are required to comply with strict anti-money-laundering

¹⁴⁸ MHA Consulting, *The Threat of Money Laundering and Terrorist Financing through the Online Gambling Industry*, report prepared for the Remote Gambling Association, June 2009, at p. 6–8.

¹⁴⁹ See *Id.* at p. 31.

¹⁵⁰ American Gaming Association, *Money Laundering*, AGA Fact Sheet, http://www.americangaming.org/Industry/factsheets/issues_detail.cfv?id=3 (last accessed on September 11, 2009).

¹⁵¹ See *Id.*

¹⁵² See *Id.*

¹⁵³ David O. Stewart, *An Analysis of Internet Gambling and Its Policy Implications*, AGA 10th Anniversary White Paper Series on Internet Gambling, 2006.

¹⁵⁴ See *Supra* at footnote 31 at p. 126–127.

procedures, which include identification of prospective customers, evidence of identity, changes to patterns of transactions, record keeping, records of transactions, retention of records, reporting suspicious transactions, and training.¹⁵⁵ In addition, site operators are legally required to report any suspicious transactions to the Financial Crime Unit (FCU). Specialized software can flag these transactions.

Similarly, to combat money laundering, Alderney requires operators of online gambling websites to implement business risk assessments, customer due diligence procedures, monitoring of transactions and other activity, suspicious activity reporting procedures, employee screening and training procedures, and record-keeping procedures.¹⁵⁶

3. Relevant Technologies for Risk Mitigation

An anti-money-laundering regulatory regime for online gambling may be modeled on the current regulatory structure for traditional bricks-and-mortar casinos. A regulatory framework for online gambling may leverage the technological environment for online gambling and require (1) preservation of an audit trail of transactions for analysis by federal authorities; (2) implementation of customer identification standards; (3) controls to prevent anonymous, structured transactions; (4) establishment of an anti-money-laundering compliance program; (5) training for all appropriate personnel; and (6) compliance with all relevant BSA requirements.¹⁵⁷

The IGC notes that “online gambling, with a combination of regulatory oversight and use of technology—while facing the same threats as real-world gambling facilities—is in a better position to address these risks.”¹⁵⁸ For example, all electronic fund transfers can be electronically recorded, thus providing a detailed and automatic transaction trail not currently available in land- and river-based casinos.¹⁵⁹

The IGC further notes that a basic requirement to combat money laundering is to “know your customer.” Stringent player registrations and ongoing verification processes combined with appropriate regulatory oversight and banking regulations help fulfill this requirement.¹⁶⁰ Italy’s regulatory regime, for example, requires a potential customer to submit a signed contract along with a copy of his or her identification.¹⁶¹ Tasmania requires strong identity verification

¹⁵⁵ See *Id.*

¹⁵⁶ See Alderney Gambling Control Commission, *The Alderney eGambling Regulations*, 2006., <http://www.gamblingcontrol.org/userfiles/file/97.pdf> (last accessed on August 19, 2009), at Schedule 6, Part VI.

¹⁵⁷ See *Id.*

¹⁵⁸ Interactive Gaming Council, “Online Gambling Sites Less Susceptible to Money Laundering Than Real-World Counterparts,” *Winner Online*, September 24, 2002, <http://www.winneronline.com/articles/september2002/fatf.htm> (last accessed on September 11, 2009).

¹⁵⁹ See *Supra* at footnote 115.

¹⁶⁰ See *Supra* at footnote 115.

¹⁶¹ As noted in an August 13, 2009 correspondence with Katharina Riedl of bwin (Austria).

procedures to be in place on player accounts.¹⁶² Moreover, technology can equip site operators with tools to scrutinize inconsistent player behavior, and then capture and report the transaction.¹⁶³

Another essential anti-money-laundering measure noted by the IGC is to require that gamblers be paid any winnings in the same way in which the money was originally deposited.¹⁶⁴ This system allows an audit to track transfers of funds much more easily and removes the ability of launderers to use an account as a pass-through for funds.¹⁶⁵ Also, care must be taken when allowing transfers of funds between players, which could potentially be a conduit for money laundering. Alderney's money laundering guidance suggests that transferred funds be allowed only for gambling and not for withdrawal or that site operators undertake further due diligence on players involved in transfers.¹⁶⁶

In addition to a system modeled on requirements for bricks-and-mortar gambling, a regulator can require the same procedures that are required of online merchants, banks, and payment providers. In Europe, online gambling operators have been bound by these requirements since 2003 under the Third European Money Laundering Directive.¹⁶⁷ U.S. licensed operators would also be bound by relevant anti-money-laundering requirements. Most nations are also subject to the recommendations of the Financial Action Task Force, an international body formed to combat money laundering and terrorist financing. Each nation may also have its own money laundering regulations, such as the United Kingdom's Money Laundering Regulations, which cover both financial and nonfinancial businesses.¹⁶⁸

Although financial businesses are still subject to the most stringent regulation, all of these regulations use a risk-based approach, in which the level of scrutiny of transactions is commensurate with the risk of money laundering in those transactions.¹⁶⁹ The most important aspects of financial companies' risk mitigation involve three broad activities: (1) "know your customer" procedures, (2) monitoring for suspicious activity, and (3) procedures for reporting suspicious activity.¹⁷⁰ Identity verification can involve both paper and electronic identification,

¹⁶² As noted in an August 5, 2009 interview with Glenn Gibson, Manager of Technical and Systems Audit at the Tasmanian Gaming Commission, and Damien Jarvis, Assistant Director of the Liquor and Gaming Branch of the Tasmania Department of Treasury and Finance (Australia).

¹⁶³ See *Id.*

¹⁶⁴ See *Supra* at footnote 158.

¹⁶⁵ See *Supra* at footnote 148 at p. 26.

¹⁶⁶ *Id.* at p. 20.

¹⁶⁷ *Id.* at p. 1.

¹⁶⁸ *Id.*

¹⁶⁹ *Id.* at p. 2.

¹⁷⁰ *Id.* at p. 29–31.

and the level of additional identification required rises with the risk in the particular industry and transaction. Suspicious activity monitoring involves standard procedures that are designed to reveal signs of monitoring while retaining privacy protection. All suspicious activity must be reported to law enforcement, which takes over the investigation immediately. Suspicious activity reporting, as part of the regulations, is the responsibility of all company staff members, who must be trained in the signs of money laundering and be able to report their suspicions expeditiously. In the United Kingdom, not reporting suspected money laundering is a criminal offense with a maximum sentence of two years in prison.¹⁷¹

4. Conclusion

Players or groups of players acting in concert may attempt to use legitimate gambling operations for money laundering. To curb such activities, regulators could subject online gambling operators to anti-money-laundering regulations that are currently in place for bricks-and-mortar casinos and for online merchants, banks, and payment providers. The online environment provides better opportunities for detecting money laundering by players or player groups than do bricks-and-mortar casinos.

In an effective anti-money-laundering regime, site operators would be required to retain comprehensive data on all deposits, withdrawals, and betting transactions and to make these available to regulators for examination and analysis. Given complete data, most patterns related to money laundering (such as light betting or matched bets placed by collaborators) would be easier to detect than they are in a physical environment (where complete transaction histories are available only in the form of video recordings).¹⁷² Software for detecting anomalies and suspicious behavior may be operated easily and routinely on digital databases by operators, regulators, or both.

The site operators' obligations with respect to their own detection of money laundering would form a part of their ordinary compliance obligations under such a licensing regime. Because of the absence of cash in online gambling transactions, the auditable record that is created, and the regulator-imposed reporting requirements for most transactions, it is likely that site operators can prevent money laundering by players and terrorist financing at least as effectively as can bricks-and-mortar casinos.¹⁷³ In contrast, the current prohibitions related to online gambling forces players to use unconventional forms of payment that leave harder-to-follow audit trails, and may therefore increase the risk of money laundering.

¹⁷¹ *Id.* at p. 23.

¹⁷² As noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority.

¹⁷³ As noted in an August 3, 2009 interview with Paul Mathews, Former Senior Vice President of IGT Wagerworks.

F. Money Laundering by Site Operators

In addition to money laundering by players, there are concerns about money laundering by site operators.¹⁷⁴ The volume, speed, and international reach of Internet transactions, along with the offshore location of many Internet gambling sites, increase the potential for misuse of these sites by operators for laundering money. As such behavior would constitute criminal conduct by site operators, effective management of the problem involves regulatory restrictions designed to keep criminals out of the Internet gambling industry.

I. The Issue of Money Laundering by Site Operators

The GAO reported in 2002 that U.S. law-enforcement officials believed money launderers might develop Internet gambling sites for the sole purpose of laundering money.¹⁷⁵ GAO cited the possibility that a gambling site operator could design software to skim a percentage of customer deposits and cloak the transactions as gaming losses. In reality these deductions would serve as the operator's service fee for laundering illicit funds. An alternate scenario might involve a gambler transferring funds to the site operator or to a collaborator within the e-casino by continuing to play until he loses the requisite amount. Conversely, if the site operator wanted to transfer funds to a gambler, the games could be rigged so the gambler won.¹⁷⁶

Two recent cases, involving NETeller and playwithal.com, highlight the possibility of online gambling operators using third-party conduits to engage in money laundering, concealing the true nature and purpose of financial transactions. In early 2007, the founders of NETeller, a popular third party payment processor based in the Isle of Man, were arrested and charged with laundering billions of dollars of Internet gambling proceeds.¹⁷⁷ In 2006, the Federal Bureau of Investigation (FBI) began investigating how NETeller processed payments and helped facilitate sports bets. NETeller used payment and shell companies to process Automatic Clearinghouse (ACH) transactions, thus hiding the nature of payments made to U.S. customers. To get money out of the United States, NETeller would have a payment service company receive funds on its behalf and transfer the funds to an account controlled by NETeller in Alberta, Canada.

In the case involving playwithal.com, a sports betting website, 27 people were charged with numerous counts, including money laundering.¹⁷⁸ The defendants were accused of laundering

¹⁷⁴ General Accounting Office, *Internet Gambling: An Overview of the Issues*, GAO-03-89, December 2002, at p. 36.

¹⁷⁵ See *Id* at p. 37.

¹⁷⁶ Testimony of John G. Malcolm Before the Committee on Banking, Housing, and Urban Affairs, March 18, 2003, <http://www.usdoj.gov/criminal/cybercrime/malcolmTestimony318.htm> (last accessed on July 29, 2009).

¹⁷⁷ Verrinder, Matthew, *NETeller Ex-directors on Money Laundering*, January 16, 2007, <http://www.reuters.com/article/internetNews/idUSN1622302920070116> (last accessed on September 11, 2009).

¹⁷⁸ Online Gambling Operations in Queens Busted, November 16, 2006, <http://online.casinocity.com/article/online-gambling-operation-in-queens-busted-68919> (last accessed on September 11, 2009).

and stashing away millions of dollars using shell corporations and bank accounts in Central America, the Caribbean, Switzerland, and Hong Kong.

2. Existing Controls in Other Jurisdictions

The United States has already enacted strict regulations to detect and deter money laundering, and site operators should clearly be forced to comply. Control strategies for this risk thus focus on keeping organized crime, other criminals and criminal behavior out of the industry.¹⁷⁹ As for all the other concerns about criminal conduct by operators, regulators will set a high bar for initial qualification and conduct periodic reviews of key personnel and their associations. Other jurisdictions do this already. The Isle of Man, U.K., and Alderney assess the suitability of license applicants and require them to submit documentation to satisfy the enforcement authorities that they are persons of good character, honesty and integrity.¹⁸⁰ Operators in these jurisdictions are also required to provide comprehensive financial statements and internal accounting records for audit.¹⁸¹

In many U.S. states, background checks and employee verification are already standard procedure for bricks-and-mortar casinos. For example, in New Jersey and Nevada, to obtain a license, each casino employee must supply his or her name, address, fingerprints, and consent to a criminal background check.¹⁸² Bricks-and-mortar casinos are also required to provide periodic financial reports at a level of detail and in formats specified by regulators.¹⁸³

3. Relevant Technologies for Risk Mitigation

Effective strategies to combat money laundering by site operators involve frequent and comprehensive auditing, the application of pattern recognition to aggregated financial transaction data, and exclusion of criminals.

¹⁷⁹ McCormick, Amanda, *Review of Online Gambling Literature*, British Columbia Center for Social Responsibility, 2007.

¹⁸⁰ Testimony of Mary Williams, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, p. 128. Also see *Supra* at footnote 128. Also see Testimony of André Wilsenach, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 140–141.

¹⁸¹ Testimony of Mary Williams, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 126–127.

¹⁸² New Jersey Permanent Statutes, Title 5, Amusements, Public Exhibitions and Meetings, 5:12-82: Casino license – applicant eligibility. Also see Nevada Revised Statutes, Chapter 463.335.

¹⁸³ See *Id* Nevada Revised Statutes at Chapter 463.156–159.

4. Conclusion

As with the prevention of fraud and any other criminal conduct by site operators, an effective regulatory regime would seek to bar criminals from entering the Internet gambling industry, and seek to detect and prevent linkages developing between site operators and criminal organizations. Regulators would also develop the capacity to search for laundering patterns among the betting transaction data, as well as among the external financial flows data for regulated sites. Regulators of the online gambling industry would also become natural partners for the broader law-enforcement community seeking to detect and prevent money laundering.

G. Violation of Jurisdictional Restrictions or Prohibitions

A key concern of some policymakers is the ability of regulated online gambling sites to adhere to various jurisdictional restrictions and prohibitions.¹⁸⁴ For example, with bricks-and-mortar casinos, some states have complete prohibitions (e.g., Utah) while others have legalized most forms of gambling (e.g., Nevada).¹⁸⁵ Add to this mix the numerous Native American tribal areas, and a complicated multilayered jurisdictional map emerges. This section does not comment on federalism or the appropriateness of various levels of jurisdictional control over online gambling. Rather, we look at the ability to ensure through federal regulation that restrictions and prohibitions imposed at various other jurisdictional levels continue to be respected.

1. The Issue of Violation of Jurisdictional Restrictions

A central issue in the debate over legalization of online gambling pertains to different jurisdictions' abilities to preclude gambling website operators from operating from, or serving customers within, specific states or territories.¹⁸⁶

Federal laws, such as the Wire Act and the UIGEA, removed some aspects of states' ability to choose legalization and regulation.¹⁸⁷ On the one hand, the passage of the UIGEA in 2006

¹⁸⁴ In October 2008, Governor Steve Beshear of Kentucky initiated a lawsuit against gambling sites serving customers in Kentucky; a court ordered 141 website domain names to be transferred to the state's control. The case was later overturned on appeal in January 2009 and is currently being appealed to the Kentucky Supreme Court. In April 2009, the state of Minnesota sent notice to 11 Internet service providers (ISPs) seeking to force them to block access to gambling sites for Minnesota residents. In June, the state rescinded its order. See *Poker News Daily*, "Minnesota Rescinds Internet Gambling Notices to ISPs after iMEGA Settlement," June 8, 2009, <http://www.pokernewsdaily.com/minnesota-rescinds-internet-gambling-notices-to-isps-after-imega-settlement-2749/> (last accessed on August 10, 2009).

¹⁸⁵ American Gaming Association, *States with Gaming*, AGA Fact Sheet, http://www.americangaming.org/Industry/factsheets/general_info_detail.cfv?id=15 (last accessed on July 21, 2009).

¹⁸⁶ Kevin F. King, "Cutting Internet Gambling's Gordian Knot: Geolocation and Federalism on the Internet," *Northwestern University Law Review*, July 14, 2009, <http://ssrn.com/abstract=1433634> (last accessed on July 20, 2009).

increased the federal government's control over online gambling and restricts users' ability to fund their online accounts, casting a broad net over any state attempts to legalize online gambling.¹⁸⁸ On the other hand, states have no recourse against offshore sites that provide gambling services to their residents.¹⁸⁹

Despite concerns that the legalization of online gambling would override various jurisdictions' rights to regulate gambling, technology can give states that opt out of legalization some assurance that their restrictions will be enforced.¹⁹⁰ A well-crafted federal regulatory regime could respect jurisdictional differences with regard to legalization of online gambling.

2. Regulatory Strategy

Proposed legislation provides for the ability of states and Native American tribal groups to opt out of legalization.¹⁹¹ A federal licensing system would need to ensure (1) that site operators "adopt and implement systems to enforce any applicable Federal, State, and Indian tribe limitations on Internet gambling" and (2) that license applicants have a program "to verify the State or tribal land in which the customer is located at the time the customer attempts to initiate a bet or wager."¹⁹² Further, currently proposed legislation prohibits licensees only from "knowingly" accepting bets from jurisdictions that opt out, presumably to prevent state actions against operators for mere negligence.¹⁹³ It would be possible to press operators further, requiring them to acquire and operate state-of-the-art methods in this area, effectively guaranteeing their "knowledge" in all but the most unusual of circumstances.

A regulatory strategy to solve jurisdictional issues must entail oversight by a regulator that can monitor site operators, including the use of mystery shopper, to ensure compliance. Beyond that, however, the issue of different jurisdictional restrictions or prohibitions is essentially a technical question: does the technology exist to implement such restrictions or prohibitions?

¹⁸⁷ See *Id.* at p. 2-5.

¹⁸⁸ See *Supra* at footnote 18 at p. 933.

¹⁸⁹ See *Id.* at p. 930.

¹⁹⁰ Spencer Bachus, "Online Gambling Leads to Crime and Hurts Young, So Why Encourage It? Asks Spencer Bachus," *US News & World Report*, June 1, 2009, <http://www.usnews.com/articles/opinion/2009/06/01/online-gambling-leads-to-crime-and-hurts-young-so-why-encourage-it-asks-spencer-bachus.html> (last accessed on July 30, 2009).

¹⁹¹ "There is a need to extend the regulatory provisions of this Act to all persons, locations, equipment, practices, and associations related to Internet gambling, with each State and Indian tribe having the ability to limit Internet gambling operators from offering Internet gambling to persons located within its territory by opting out of the provisions of this Act" (Internet Gambling Regulation, Consumer Protection, and Enforcement Act, H.R. 2267, 111th Cong. (2009), §5381, ¶6).

¹⁹² See *Id.* at §5381, ¶5. Also see *Id.* at §5384(b)(1).

¹⁹³ See *Id.* at §5386(a)(1)(A). Also see *Supra* at footnote 186 at p. 17.

3. Relevant Technologies for Risk Mitigation

Many technologies are available to mitigate the risks of jurisdictional violations of restrictions or prohibitions.

To adhere to UIGEA restrictions that prohibit funding of online gambling accounts, some overseas gambling operators, such as PartyGaming, Sportingbet, and Paradise Poker, have used geolocation techniques to selectively deny services to their customers on the basis of their location within the United States.¹⁹⁴ Similar technology may also be applied to help address the problem of jurisdictional differences in gambling law within the United States.

Geolocation entails using "Internet infrastructure information to determine the geographic location of Internet Protocol (IP) addresses associated with Internet-connected devices."¹⁹⁵ It is a way of determining the physical location of an Internet user, with varying degrees of accuracy. When an Internet user types a website address into a Web browser, the browser sends an access request to the server of the requested website. This request reveals the IP address of the user, which the requested website forwards to a geolocation provider. The provider, which has built a database of the locations of IP addresses, assesses the location of the user. Public-source geolocation data can often identify the location of IP addresses at the country, state, and even city levels.¹⁹⁶

Gambling websites would, of course, require initial registration information from their users, including the users' name and address. This is the first line of defense against jurisdictional concerns, because a person attempting to register with a Utah address, for example, would be precluded from opening an account.¹⁹⁷ This information can be cross-checked against supplied information, such as credit card information, bank account numbers, driver's license details, or passport information to determine any mismatch in the reported location.¹⁹⁸ Players from excluded jurisdictions, or ones whose physical location cannot be verified, can summarily be prevented from opening an account.

This process should serve as a deterrent to casual users in prohibited jurisdictions who do not intend to circumvent the laws of their jurisdiction. Subsequently, however, the site must use geolocation to ensure that users, even if they were eligible at registration, are in a permitted

¹⁹⁴ See *Supra* at footnote 60, at ¶¶34–36.

¹⁹⁵ Quova, *The Factors of Geolocation*, iGaming Business, <http://gw.vtrenz.net/index.cfm?method=cMicrositeSecurity.displayLogin&dkey=XOV3IU9JU5> (last accessed on July 21, 2009).

¹⁹⁶ D. J. B. Svantesson, "How Does the Accuracy of Geo-Location Technologies Affect the Law?" *Masaryk University Journal of Law and Technology*, 2, No. 1 (Summer 2008): 11–21, at p. 12.

¹⁹⁷ Assuming that the state of Utah, which currently prohibits gambling, would continue to do so under a federal regulatory regime.

¹⁹⁸ As noted in an August 21, 2009 interview with Andrew Fritchie, General Counsel of PartyGaming PLC.

jurisdiction while gambling. Geolocation software can pinpoint the user's location and, if in doubt, flag it for site operators to either further investigate or block access immediately.

Critics of geolocation claim that it is inherently unreliable and subject to relatively easy circumvention, citing failure rates in the range of 20% to 30%.¹⁹⁹ For example, a wireless access card, a common method of accessing the Internet on a laptop while traveling, may confuse geolocation services, and each service may show the user to be in highly disparate locations.²⁰⁰ The online gambling firm bwin uses a geolocation service, and although the company believes that the service can reliably determine the country in which a player is located, it does not currently rely on results at a state or city level.²⁰¹ Supporters and geolocation companies themselves, however, insist that the technology is highly accurate. Quova, a market leader in geolocation technology, claimed virtually 100% accuracy in helping Ladbrokes, the world's largest bookmaker, to block Dutch users from accessing its site.²⁰² Other estimates of accuracy run from 85% to 99%.²⁰³

Geolocation technology is already used for a number of purposes, such as restricting access to content, protecting media rights, and delivering location-based content to users. It is used by organizations such as the New York State Lottery, the British Columbia Lottery, Major League Baseball, and the Alaska Permanent Fund.²⁰⁴ It is also used to detect and deter fraud at online retailers by comparing the user's location with his or her credit card address, for example, and governments and law enforcement agencies use geolocation to help track Internet criminals.²⁰⁵

Technologies to circumvent geolocation do exist, such as "overt and transparent proxies, firewalls, filters and filtering services, Network Address Translators, private address spaces, point-to-point links, tunnels, and Virtual Private Networks (VPNs), that further-obfuscate the

¹⁹⁹ Statement of Jeff Schmidt, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 18-19.

²⁰⁰ See *Id.*

²⁰¹ As noted in an August 13, 2009 correspondence with Katharina Riedl of bwin (Austria).

²⁰² A Dutch court had ordered Ladbrokes, a U.K. bookmaker, to prevent domestic users from accessing its site. See *Supra* at footnote 195.

²⁰³ See *Supra* at footnote 186 at p. 15.

²⁰⁴ See *Supra* at footnote 40 at p. 53. Also see Larry Barrett, "Major League Baseball Struggles to Reach Fans Online," *Baseline*, March 7, 2005, http://www.baselinemag.com/index2.php?option=content&do_pdf=1&id=3506 (last accessed on September 4, 2009). Also see Quova, *Quova Helps the Alaska Permanent Fund Dividend Division Run Like a Well-Oiled Machine*, Quova case study, 2008, https://www.vtrenz.net/imaeds/ownerassets/818/08277_Alaska_casestudy_REV2.pdf (last accessed on September 10, 2009).

²⁰⁵ Quova, *The Science of Geolocation*, <http://www.quova.com/Technology/thescienceofgeolocation.aspx> (last accessed on September 4, 2009).

true source and destination of communications.”²⁰⁶ In some cases, the user could be on a different continent from the one indicated by their IP address because he or she may be using one of the above technologies that masks the true location. VPN programs, which many people use to access work networks from home or while traveling, effectively mask one’s location. In fact, many gateways to the Internet, such as America Online or proxy servers, by their nature offer geographic separation between the IP address and the end user.²⁰⁷

Geolocation software, however, can exploit the physical characteristics of the connection, such as the round-trip delay, to detect these countermeasures and assign a “confidence factor,” indicating the probability that the reported location is the user’s actual location.²⁰⁸ Also, the software can determine if the destination address belongs to a cable company, a DSL provider, or a dial-up ISP. Thus, the destination can indicate the user’s connection type and whether it is too risky to accurately verify the user’s location.²⁰⁹ In these cases, the customer’s account can be blocked completely from using the service until his or her location can be determined with greater certainty, or the site’s compliance department can flag the account for further review. Further review could involve requiring the user to submit additional information, which then may be subject to manual or real-time verification.²¹⁰

The regulator may impose specific requirements on the confidence of any geolocation information, on the basis of the confidence factor determined by the software, in essence to “tune” the thresholds for acceptance, rejection, and further verification.²¹¹ For example, the New York Lottery and the British Columbia Lottery use Aristotle’s verification service for geolocation. Both organizations require nearly 100% confidence scores in order to allow users to participate in their respective lotteries.²¹² In this way, regulators can have as much assurance as they require in the geolocation system, making it an effective means of excluding individuals in any specific jurisdiction.

4. Conclusion

Beyond the issue of sanctions, licensed sites may have an incentive to be lax with geolocation controls: excluding users from certain states lowers their overall customer base. Therefore, a

²⁰⁶ See *Supra* at footnote 199 at p. 83.

²⁰⁷ As noted in an August 21, 2009 interview with Andrew Fritchie, General Counsel of PartyGaming PLC.

²⁰⁸ Quova, *GeoPoint by Quova*, white paper, July 2006, https://www1.vtrenz.net/imarkownerfiles/ownerassets/818/GeoPointbyQuova_WHITEPAPER.pdf (last accessed on July 21, 2009), at p. 7.

²⁰⁹ See *Supra* at footnote 195.

²¹⁰ See *Id.*

²¹¹ As noted in an August 3, 2009 interview with Paul Mathews, Former Senior Vice President of IGT Wagerworks. Also see *Supra* at footnote 162.

²¹² See *Supra* at footnote 40 at p. 53.

regulator must ensure that geolocation controls are updated frequently and meet desired standards of quality. Frequent mystery shopping at U.S. sites conducted from locations within restricted states is one option, and violators could risk losing their valuable operating license if they chose to operate lax verification techniques. This combination of oversight and state-of-the-art technology should help ensure that various jurisdictions maintain control over their own gambling laws and prevent complex interstate legal disputes.

H. Breaches of Data Confidentiality

Online gambling websites often hold personal and confidential information of their customers, including credit card and bank account numbers, names, addresses, and other sensitive information. One of the challenges for a regulator is to ensure that personal information is used only for legitimate purposes and is not disseminated or accessed improperly.

1. The Issue of Data Confidentiality

All online businesses involved in monetary transactions are susceptible to breaches of data confidentiality.²¹³ Breaches can include hackers stealing credit card or other personal information, employees storing or accessing sensitive information improperly, and sites accidentally releasing personal information.²¹⁴ Although the deliberate theft of data is a significant problem, more than 88% of all cases of data breaches in 2008 resulted from insiders' negligence.²¹⁵ Once released, the data can then be used for various illegal purposes and may lead to identity theft and credit card fraud.

Unlike other countries, the United States does not maintain any general data privacy laws at a federal level.²¹⁶ Instead, individual states have wide latitude to enact laws protecting consumers' data, and currently 45 states have laws governing data breaches by companies.²¹⁷ Online

²¹³ In January 2009, Heartland Payment Systems, the United States' fifth-largest payment processor, announced a data breach caused by hackers that may have compromised up to 100 million credit cards. TJX, a major operator of retail stores, experienced a data breach in 2006 that exposed tens of millions of cards. See Rachel King, "Lessons from the Data Breach at Heartland," *Business Week*, July 7, 2009, <http://www.msnbc.msn.com/id/31778540/ns/business-businessweekcom/> (last accessed on July 29, 2009).

²¹⁴ *Identity Theft Daily*, "Identity Theft News: 2008 Data Breach Count is 69% greater than 2007," *Identify Theft Daily*, <http://www.identitytheftdaily.com/index.php/20080716371/Latest/Identity-Theft-News-2008-Data-Breach-count-is-69-greater-than-2007.html> (last accessed on July 29, 2009).

²¹⁵ PGP Corporation, *2008 Annual Study: Cost of a Data Breach*, conducted by the Ponemon Institute, LLC, February 2009, at p. 5, http://www.encryptionreports.com/download/Ponemon_COB_2008_US_090201.pdf (last accessed on July 31, 2009).

²¹⁶ Dan Kaplan, "Leahy, for Third Time, Submits Federal Data Security Law," *SC Magazine*, July 24, 2009, <http://www.scmagazineus.com/Leahy-for-third-time-submits-federal-data-security-law/article/140604/> (last accessed on July 29, 2009).

²¹⁷ See *Id.* Also see National Conference of State Legislatures, *State Security Breach Notification Laws*, as of July 27, 2009, <http://www.ncsl.org/Default.aspx?TabId=13489> (last accessed on September 10, 2009).

gamblers residing in the United States currently have no protection against breaches of their personal data beyond those implemented by the online gambling site itself.

2. Existing Controls in Other Jurisdictions

In 2003, California became the first state to pass a comprehensive law on notification of data breaches. The law requires companies that experience a breach to notify all data subjects “in the most expedient time possible and without unreasonable delay” if certain types of personal information are released unintentionally. It is important to note that the data must have been unencrypted to trigger the notification.²¹⁸

A 2009 bill proposed by Senator Patrick Leahy of Vermont, dubbed the Personal Data Privacy and Security Act, aims to “require data brokers and companies to establish and implement data privacy and security programs.”²¹⁹ Leahy notes that more than 250 million records containing personal information have been breached since 2005.²²⁰ The law would require companies that store customers’ personal data to establish internal control policies and to give notice when a breach of data occurs. The bill would preempt state laws on these matters.²²¹ It also would establish an Office of Federal Identity Protection to assist consumers with issues of identity theft and data correction.²²²

In Europe, most data privacy laws are highly stringent—much more so than in the United States. The European Union’s Data Protection Directive, issued in 1995, introduced strong controls on data privacy and the rights of consumers.²²³ Among other provisions, it requires that data be relevant to the purpose for which it is kept, stored no longer than necessary, and verifiable by consumers. It also requires that, if data are to be processed (i.e., collected and used), (1) the data subject should have given explicit consent for its use and (2) the processing must be necessary for the performance of a contract, required by a legal obligation, necessary to protect the data subject’s life, or necessary to perform a task of public interest.

Various jurisdictions across the world that have legalized and regulated online gambling maintain rules on data confidentiality and privacy:

²¹⁸ See California Office of Privacy Protection, “Recommended Practices on Notice of Security Breach Involving Personal Information,” May 2008, http://www.oisp.pp.ca.gov/consumer_privacy/pdf/secbreach.pdf (last accessed on July 31, 2009), at p. 8.

²¹⁹ Office of Senator Patrick Leahy, *Leahy Introduces Cybersecurity Legislation*, July 22, 2009, <http://leahy.senate.gov/press/200907/072209b.html> (last accessed on July 29, 2009), at p. 1.

²²⁰ See *Id.*

²²¹ See *Id.* at p. 5-8.

²²² See *Id.* at p. 9.

²²³ *Data Protection in the European Union*, European Commission, United Kingdom, http://ec.europa.eu/justice_home/fsj/privacy/docs/guide/guide-ukingdom_en.pdf (last accessed on September 10, 2009).

- The Isle of Man's gambling regulations "specify detailed rules on the way accounts must be managed, privacy of information on account holders and prescribe the penalty for contravention which is £5,000 for each violation."²²⁴ Site operators in the Isle of Man are also bound to the rules in the Data Protection Act 2002, the island's legislation concerning data privacy. One of the Act's provisions provides for compensation for "[a]n individual who suffers damage by reason of any contravention by a data controller of any of the requirements of this Act."²²⁵
- Jersey's regulatory system requires that "[c]ustomer privacy and data protection principles are observed."²²⁶
- Gibraltar requires that information about a player not be disclosed to a third party except under certain circumstances.²²⁷ Gibraltar's regulator also requires that data be obtained lawfully, kept and used only for the purposes for which it was obtained, stored safely, and accessible by the customer.²²⁸

3. Relevant Technologies for Risk Mitigation

Effective data protection begins with the establishment of internal controls and policies by the gambling website. Betting site 888.com states in its privacy policy that it is "committed to respecting your privacy and to complying with applicable data protection and privacy laws and we have therefore provided this Privacy Policy to help you understand how we collect, use and safeguard your PII [personally identifiable information]."²²⁹ It also states that the site's employees and data processors have an obligation to respect users' privacy. Betfair's privacy policy claims the site "endeavour[s] to ensure that [its] business practices that involve the use of...Personal Information are compliant with privacy regulations in the countries where [it] operate[s]," and it claims that it has assembled a "world class Information Security Management System."²³⁰

²²⁴ See *Supra* at footnote 31 at p. 126.

²²⁵ Data Protection Act 2002, Treasury of the Isle of Man, at §11(1).

²²⁶ See *Supra* at footnote 30 at p. 144.

²²⁷ See *Supra* at footnote 133 at §30.

²²⁸ See *Supra* at footnote 32 at p. 16.

²²⁹ See <http://www.888.com/>, under "Privacy Policy for Users" (last accessed on September 10, 2009).

²³⁰ See <http://content.betfair.com/aboutus/?product=exchange&brand=betfair®ion=GBR&locale=en> (last accessed on September 10, 2009).

Maintaining secure computer systems is a demanding task. Although the various technological solutions—secure operating systems, file encryption, network firewalls—have their weaknesses the primary failure mechanism for data security is human mistakes and carelessness.²³¹

Absent regulation, gaming site operators would not bear many of the costs associated with the improper disclosure of personal information. Thus, a regulatory mechanism is needed to align the operator's incentives with those of consumers. A significant fine for each consumer record improperly released is one such incentive.

With the proper incentives, the gaming site operator will engage in the security engineering, training of staff, and auditing needed to protect consumer records.

4. Conclusion

In an effective regulatory regime, the regulator would require the internal controls and privacy policies described in this section to be present on gambling websites and be highly visible to customers. The regulator would ensure that employees receive training in relevant data protection policies and that players have the ability to access and, if necessary, modify their personal information. It would also establish the types of data that can be stored and the length of time after which the data must be deleted. Finally, the regulatory regime may impose criminal or civil liability on site operators whose data is breached, and it can require regular audits, either by the regulator itself or by independent third parties, of data encryption policies and other protection systems. There is no reason to believe that licensed online gambling operators would be any less able or willing to fulfill these obligations than other online merchants with similar data custody obligations. For more discussion on technological strategies to protect sites' integrity and customers' personal data, see Section I, Communications and Computer Security Failures.

I. Communications and Computer Security Failures

Security of websites, to prevent improper use of or access to sensitive data, is a ubiquitous and serious concern in e-commerce. Hackers can undermine site security, alter a site's behavior, shut it down, access customers' confidential information, or use one site as a platform from which to launch broader malicious activities across the web. Online gambling sites would be responsible, in just the same way as other merchant sites, for implementing proper controls and in cooperating with law enforcement agencies in the control of cybercrime.

1. The Issue of Communications and Computer Security Failures

Web server security can be compromised from two directions. The first is over the network (i.e. through internet connections). Second, and perhaps more importantly, a website's servers are also subject to attack or misuse by the gaming site's own employees. A key employee may be able to install software that subverts a system, destroys the integrity of games, interferes with

²³¹ See Ross Anderson, *Security Engineering, A Guide to Building Dependable Distributed Systems* 2nd Edition, Wiley, 2008, at p. 17-62.

customer accounts, or improperly transmits customers' personal or financial information. Even an ordinary virus may render a site inoperative, making it impossible for customers to access their accounts or recover their deposits. Phishing attacks, directed at customers through a gambling website, may also be a concern.

Attacks may involve unauthorized attempts to login using someone else's account, or exploitation of some security weakness in the web server software itself or in the communications software on the server.²³²

Protecting gaming websites from intruders is little different from the problem faced by government agencies or online merchants such as Amazon. Many organizations do this quite well as a matter of course, and licensed gambling site operators should be held to a high standard.

There are currently no U.S. federal laws regarding data breaches, and the issue is left to individual states. However, acts of hacking and computer fraud are addressed by the Computer Fraud and Abuse Act, originally enacted in 1986, which covers any interstate or international computer communications.²³³ The Act criminalizes a wide range of computer fraud, including improperly accessing a "protected" computer with intent to defraud and knowingly transmitting a program or code that causes damage to multiple computers. A 2008 amendment to the law eliminated the requirement for the communications to be interstate or international in cases involving theft and broadened the definition of a "protected computer" to mean any computer used in interstate or foreign communication.

Like other heavily-used websites, gambling sites are susceptible to denial-of-service attacks, which overload a website's servers and force it to shut down.²³⁴ The threat of such attacks has been used to extort money from website operators. Perpetrators of such extortion have included organized crime groups from the Middle East and Asia.²³⁵ In 2004, British bookmakers alone lost \$70 million due to "cyber-extortion" by just one hacking team, and companies such as

²³² For a description of a recent (September 2009) discovery of a security weakness in web server software, see Gregg Keizer, *Microsoft promises patch for critical Web server bug*, Computerworld, September 2, 2009, http://www.computerworld.com/s/article/9137438/Microsoft_promises_patch_for_critical_Web_server_bug (last accessed on September 9, 2009).

²³³ See U.S. Department of Justice, *Chapter 1 – Computer Fraud and Abuse Act*, Computer Crime & Intellectual Property Section, <http://www.usdoj.gov/criminal/cybercrime/ccmanual/01ccma.pdf> (last accessed on July 29, 2009).

²³⁴ Denial-of-service attacks use computers to inundate a website with large amounts of internet traffic that eventually slows the site or shuts it down completely. See Jack M. Germain, "Global Extortion: Online Gambling and Organized Hacking," *Tech News World*, March 23, 2004, <http://www.technewsworld.com/story/33171.html?wlc=1248627730> (last accessed on July 26, 2009). Also see Jordan Robertson, "Tech 101: How a Denial-of-Service Attack Works," *Associated Press*, July 8, 2009, <http://www.usnews.com/articles/science/2009/07/08/tech-101-how-a-denial-of-service-attack-works.html?PageNr=1> (last accessed on July 28, 2009).

²³⁵ See *Id.*

Canbet, Harrods Casino, Inter Casino Poker, Totalbet, VIP Casino, and William Hill have been the victims of denial-of-service attacks.²³⁶

Users of gambling websites are also susceptible to phishing, or the use of fraudulent but credible-looking website-mimics to deceive the user into releasing personal information or to install viruses and other malware onto their computers.²³⁷ Phishing may take many forms including fraudulent or misleading email, website pop-up advertisements, or other forms of electronic communication such as text messaging. Phishing attacks cost consumers more than \$3 billion annually in the form of fraudulent credit card charges, withdrawals from compromised bank accounts, time spent rectifying fraud problems, and reduced trust in online commerce.²³⁸ Depending upon factors such as the website's payout policy or the ability to transfer funds between players, gambling websites can be attractive targets for phishing.²³⁹

2. Existing Controls in Other Jurisdictions

In a licensed regulatory environment, gambling site operators would be expected to play their part—just like any other e-commerce merchant—in eliminating their own security vulnerabilities and cooperating with law-enforcement agencies in cybercrime control. Existing U.S. laws (federal and state) regarding computer intrusion would apply, and sites would have recourse to law enforcement support if they suffered attacks. Other nations have legal regimes similar to the U.S. with respect to cybercrime. France, Germany, and the United Kingdom all have laws specifically targeting cybercrime, and the European Union is currently looking to both strengthen its laws on cybersecurity and harmonize the laws of its member states.²⁴⁰ The European Union is also considering a system through which members can report Internet-based attacks to each other and record arrests and prosecutions.²⁴¹ The Licensing, Regulation, and Alcohol Strategy division

²³⁶ See John McMullan and Aunshul Rege, *Cheating and Cybercrimes @ Gambling Sites.com*, presentation to the Alberta Gambling Research Institute Annual Conference, March 2009, slide 17. Also see John McMullan and David Perrier, "The Security of Gambling and Gambling with Security: Hacking, Law Enforcement and Public Policy," *International Gambling Studies* 7, No. 1 (2007): 43–58 at p. 47.

²³⁷ Rachna Dhamija *et al.*, *Why Phishing Works*, Experimental Social Science Laboratory (Xlab), Paper XL06-013 (August 14, 2006): 581–590 at p. 581, <http://repositories.cdlib.org/iber/xlab/XL06-013> (last accessed on August 3, 2009). Also see Cyveillance, *The Cost of Phishing: Understanding the True Cost Dynamics Behind Phishing Attacks*, white paper, December 2008, http://www.cyveillance.com/web/docs/WP_CostofPhishing.pdf (last accessed on August 3, 2009). Also see APWG, *Phishing Activity Trends Report Q1/2008*, January–March 2008, http://www.antiphishing.org/reports/apwg_report_Q1_2008.pdf (last accessed on August 3, 2009).

²³⁸ See *Id.* Cyveillance.

²³⁹ Marvin Fabuli, "Online Casinos an Easy Bet for Phishers," Symantec, February 27, 2008, <http://www.symantec.com/connect/blogs/online-casinos-easy-bet-phishers> (last accessed on August 3, 2009).

²⁴⁰ Palmer, Maija, "EU plans tougher cybercrime laws," *FT.com*, June 14, 2009, <http://www.ft.com/cms/s/0/10a407b6-5913-11de-80b3-00144feabdc0.html> (last accessed on August 2, 2009).

²⁴¹ See *Id.*

in Australia's Northern Territory requires license applicants to submit their information technology security protocols for a risk assessment, and their controls must adhere to Australian and New Zealand AS/NZS 4444 standards for information security.²⁴²

The issue of hacking is not completely unfamiliar to bricks-and-mortar casinos. They use quite sophisticated electronic systems, which are vulnerable as well.²⁴³ A regulatory strategy for online gambling would require implementation and maintenance of state-of-the-art security controls, cooperation with law-enforcement on cybercrime issues, comprehensive testing of site and account security for the sake of defending consumers' privacy and interests, and mandatory reporting of any attacks.²⁴⁴

3. Relevant Technologies for Risk Mitigation

The key technologies for gambling website security are the same as those used by other on-line merchants. These include (1) network firewalls that isolate databases, administrative systems, and development systems from the Internet, (2) high-quality servers with up-to-date security patches, (3) a continuing process of monitoring and logging attempts to break into the system over the Internet, (4) secure database and transactional software, and (5) the use of secure, encrypted protocols for communications between users and the gambling website.²⁴⁵

Intruders who gain access to a user's credentials and use those credentials to open a fraudulent connection can be combated in several ways. Many gambling sites work by having users download and install dedicated client software to access the site rather than relying on standard web browsers. This dedicated client software can implement security protocols that resist a variety of exploits such as keystroke loggers and "man-in-the-middle" attacks.²⁴⁶ For example, the gambling site could use encryption keys based, in part, on information exchanged at registration and stored on the user's computer. This approach, however, is not as user friendly as a simple login (e.g., user name and password), as it would make the use of any computer other than the user's regular computer more difficult.

²⁴² As noted in an August 31, 2009 correspondence with John Sealy, Manager of Information Systems and Technology Services at the Licensing, Regulation and Alcohol Strategy division of the Northern Territory Department of Justice (Australia).

²⁴³ See John McMullan and David Perrier, "The Security of Gambling and Gambling with Security: Hacking, Law Enforcement and Public Policy," *International Gambling Studies* 7, No. 1 (2007): 43-58 at p. 44.

²⁴⁴ See *Id.* at p. 53.

²⁴⁵ Keys Botzum, WebSphere Application Server V6 advanced security hardening -- Part 1, Overview and approach to security hardening, IBM WebSphere Developer Technical Journal, December 2005, http://www.ibm.com/developerworks/websphere/techjournal/0512_botzum/0512_botzum1.html (last accessed on September 14, 2009)

²⁴⁶ Keystroke loggers are programs that record users' keystrokes for the purpose of garnering private information such as passwords. "Man-in-the-middle" attacks are cryptographic attacks in which an eavesdropper relays messages between two victims. The eavesdropper can read and even alter the messages.

Another approach is to add a feature to the user's password. It is common for high-value websites to put an additional password on a physical device, such as a small keyfob that displays a six-digit number that changes once per minute.²⁴⁷ The user logs in by supplying the user name, password, and the number on the fob, and these are passed through to the server, which authenticates them and permits the user to log in. This technology protects against lost and easy-to-guess passwords but not against man-in-the-middle attacks. However, if the site requires the user to employ dedicated client software, that client software can use the 6-digit number as part of the encryption key for establishing the connection between the user's computer and the web server; this technique would successfully protect against man-in-the-middle attacks.²⁴⁸

Gambling site operators are already aware of some of these options. For example, PartyGaming's privacy policy states that it stores all players' personal information in a password-protected database behind a state-of-the-art firewall, and the site itself supports SSL version 3 security with 128-bit encryption.²⁴⁹ It also states that it ensures that affiliates, subsidiaries, agents, and suppliers use secure technology. The site 888.com claims that it uses advanced SSL and PGP protocols for security along with public/private key encryption and firewalls.²⁵⁰ Both sites employ secure, dedicated client software. Other gambling sites also enumerate details about their security policies and procedures, all of which are designed to prevent unauthorized access to personal information.

Denial-of-service attacks present a particular challenge to gaming site operators. The harmful traffic usually arises from thousands or tens of thousands of computers that have been infected with a virus that permits the author of the virus to remotely control the infected computer. The individual commanding such a network can direct the entire network to begin loading pages from the gambling website. If the website is designed to serve a thousand active users but ten thousand computers begin loading web pages at ten times the rate of a normal user, service from the website could collapse.

Some technological countermeasures are available to the website operator—for example the website could place limits on the number of new computers from which it will accept connections. However, if the flow of incoming traffic is big enough it will overload the connections between the gambling site and the rest of the Internet. Thus, the ultimate control of denial-of-service attacks must come from web administrators, providers of operating system software, and network service providers.

²⁴⁷ This process is called two-factor authentication. One factor is the normal password which the user types, and the other is the code from the key fob. The interactive role-playing game service World of Warcraft provides such key fobs to its users for a fee of \$6.50. See <http://www.blizzard.com/store/details.xml?id=1100000622> (last accessed on September 9, 2009).

²⁴⁸ If the 6-digits are used as a shared secret to generate part or all of the encryption key for the communications between the user and the game site, then a man-in-the-middle attack is impossible because the attacker lacks the shared secret.

²⁴⁹ See https://secure.partyaccount.com/about/privacy_s.do (last accessed on August 24, 2009).

²⁵⁰ See <http://www.888.com/> (last accessed on August 24, 2009).

Security failures in computer operating systems are the gateway through which most viruses infect computers. Network service providers have the ability to monitor traffic flows on many different paths and can detect patterns of activity that indicate the beginnings of a denial-of-service attack. They may also be able to control denial-of-service attacks at locations far from the connection to the gambling site.

For this reason, sites must work closely with regulators and government agencies to identify and deal with cybercriminals. Regulators should develop cooperative relationships with private security experts and advocate for cost-effective, industry-wide benchmarks for cyber-security.²⁵¹ Finally, legislators should consider imposing civil liability on site operators for any harm caused by computer intrusions, at least when site security precautions were not up to the requisite standard.²⁵²

Finally, gambling site operators, like all other online merchants, should implement anti-phishing measures to prevent financial harm to consumers and maintain the integrity of their operations. The sites should play their role in helping to educate consumers about safe browsing habits and how to recognize phishing.²⁵³

4. Conclusion

Significant international attention is already being paid to cybercrime in general. Website security is a matter of global concern for businesses and government alike, by no means specific to online gambling. According to a Cyberspace Policy Review report released in 2009 by the Cybersecurity Chief at the National Security Council, "a growing array of state and non-state actors are compromising, stealing, changing, or destroying information and could cause critical disruptions to U.S. systems."²⁵⁴ The report recommends a coordinated effort by federal, state, and local governments along with security experts in the private sector, and it urges the government to "identify procurement strategies that will incentivize the market to make more secure products and services available to the public."²⁵⁵ It goes on to recommend "adjustments to liability considerations (reduced liability in exchange for improved security or increased

²⁵¹ See John McMullan and Aunshul Rege, *Cheating and Cybercrimes @ Gambling Sites.com*, presentation to the Alberta Gambling Research Institute Annual Conference, March 2009, slide 23.

²⁵² John McMullan and David Perrier, "The Security of Gambling and Gambling with Security: Hacking, Law Enforcement and Public Policy," *International Gambling Studies* 7, No. 1 (2007): 43-58 at p. 56.

²⁵³ MarkMonitor, "Rock Phishing: The Threat and Recommended Countermeasures," White Paper, August 2007, <http://www.markmonitor.com/download/wp/wp-rockphish.pdf> (last accessed on August 3, 2009), at p. 7-8.

²⁵⁴ Cyberspace Policy Review, *Assuring a Trusted and Resilient Information and Communications Infrastructure*, National Security Council, May 2009, <http://www.whitehouse.gov/asset.aspx?AssetId=1906> (last accessed on August 2, 2009), p. iii. Also see <http://www.whitehouse.gov/cyberreview/>.

²⁵⁵ See *Id* at p. iv-v.

liability for the consequences of poor security), indemnification, tax incentives, and new regulatory requirements and compliance mechanisms.”²⁵⁶

While all online merchants would benefit from increased governmental and law enforcement support, online gambling operators are ultimately responsible for their own sites’ security. Site operators will naturally be concerned with their reputations for integrity and reliability, but regulation can introduce new incentives to ensure that operators deploy effective security. The regulator might choose to mandate some specific technologies, such as SSL encryption and dedicated client software; and it can sharpen the incentives for effective control by imposing higher levels of liability for any sites that fail to implement adequate precautions.

J. Problem Gambling

1. Problem Gambling

We expect that problem gambling behaviors may receive more attention in the upcoming debates than any of the other categories of risk. Therefore, we discuss problem gambling in more detail in Section III below.

²⁵⁶ See *Id* at p. v.

III. SPECIAL ATTENTION TO PROBLEM GAMBLING

A. Introduction

Unlike the other nine risks, the potential effect of legalization on problem gambling is less obvious a priori. On the one hand, in a well-regulated online environment, gamblers (including existing U.S.-based online gamblers) would have more access to mechanisms with which to try to curb their problem behavior. These include tools for self-exclusion and self-limits as well as greater awareness of and access to clinical and self-help resources. On the other hand, pathological or addictive gambling behaviors might nevertheless be exacerbated by the increased opportunity to gamble at any time and from anywhere.

B. What is Problem Gambling?

1. Terminology

Problem gambling is a term without a specific definition that refers to the fact that some individuals who gamble do so irresponsibly and damage or disrupt personal, financial, or social pursuits.²⁵⁷ The term can apply to a wide spectrum of cases, from less severe ones where individuals experience some degree of gambling-related problems to more severe cases in which individuals are clinically diagnosed with *pathological gambling*—an impulse control disorder.²⁵⁸

²⁵⁷ Lack of specific definition noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority. National Council on Problem Gambling, *FAQs – Problem Gamblers*, <http://www.ncpgambling.org/i4a/pages/Index.cfm?pageID=3315> (last accessed on July 11, 2009).

²⁵⁸ In 1980, the American Psychiatric Association (APA) first included pathological gambling in the Diagnostic and Statistical Manual for Mental Disorders (DSM). It was described as a “chronic and progressive failure to resist impulses to gamble, characterized by undesirable outcomes ranging from borrowing money from family or friends and losing time at work, to being arrested for offenses committed to support gambling.” National Research Council, *Pathological Gambling: A Critical Review*, Washington, DC: National Academy Press (2005), at p. 2. In the most current manual, DSM-IV, the APA lists 10 diagnostic criteria of which five have to be met to make a clinical diagnosis of pathological gambling. See *Id* at p. 27. Various screening mechanisms have been developed to assess levels of problem gambling, including the South Oaks Gambling Screen (SOGS), the Problem Gambling Severity Index (PGSI) of the Canadian Problem Gambling Index (CPGI), and the National Opinion Research Center DSM Screen for Gambling Problems (NODS). See Michael Belletire *et al.*, *Legislating and Regulating Casino Gaming: A View from State Regulators*, paper commissioned by the Regulation, Enforcement and Internet Subcommittee of the National Gambling Impact Study Commission, 1999, at p. 11. Also noted in interviews with Peter Collins, Professor of Public Policy Studies and Director of the Center for the Study of Gambling at the University of Salford (U.K.), and Sam McQuade, Graduate Program Coordinator at the College of Applied Science and Technology at the Rochester Institute of Technology.

2. Prevalence Rates and Trends

Worldwide: Most research indicates that about 1% of the adult population worldwide experiences severe problem gambling.²⁵⁹ Moreover, studies indicate that severe problem gambling rates globally have stabilized over time at about 1%.²⁶⁰

United States: Various studies have been conducted to estimate the prevalence of problem gambling in the United States. According to the National Council on Problem Gambling, about 1% of the U.S. adult population meets the criteria for pathological gambling in a given year. Another 2% to 3% would be considered problem gamblers.²⁶¹ In a meta-analysis of 120 previously conducted prevalence studies in the United States and Canada, researchers at the Division of Addictions at Harvard Medical School derived point-in-time estimates of problem gambling rates. They noted that 1% to 2% of the adult population met criteria for lifetime pathological gambling.²⁶² A more recent estimate from a nationally representative survey in the United States found lifetime pathological gambling rates within the general population of 0.4%.²⁶³ In an interview in mid 2009, Howard J. Shaffer, an addiction expert at Harvard University, noted that despite the substantial growth in gambling opportunities and overall gambling volume over the last two decades in the United States, the rate of problem gambling among the adult population has stayed roughly constant. Shaffer also stated that the incidence of problem gambling in the United States had declined slightly since the 1970s, from 0.7% to 0.6%.²⁶⁴

Online Gambling and the Incidence of Problem Gambling: Some studies have claimed an association between increased gambling exposure and increased incidence of problem

²⁵⁹ Jamie Wiebe *et al.*, *Problem Gambling Prevalence Research: A Critical Overview*, a report to the Canadian Gaming Association, December 2007, at p. 2, http://canadiangamingassociation.com/media_uploads/pdf/78.pdf (last accessed on September 10, 2009).

²⁶⁰ See *Id.* Also see D. A. LaPlante and H. J. Shaffer, "Understanding the Influence of Gambling Opportunities: Expanding Exposure Models to Include Adaptation," *American Journal of Orthopsychiatry*, 77, No. 4 (2007): 616–623 at p. 619.

²⁶¹ See *Supra* at footnote 257. Also noted in a June 5, 2009 interview with Keith Whyte, Executive Director of the National Council on Problem Gambling.

²⁶² Howard Shaffer *et al.*, "Updating and Refining Prevalence Estimates of Disordered Gambling Behaviour in the United States and Canada," *Canadian Journal of Public Health*, 92, No. 3 (2001): 168–172 at p. 169. Also see Howard Shaffer *et al.*, *Estimating the Prevalence of Disordered Gambling Behavior in the United States and Canada: A Meta-Analysis*, Boston: Presidents and Fellows of Harvard College, 1997, at p. iii. Also see Howard Shaffer *et al.*, "Estimating the Prevalence of Disordered Gambling Behavior in the United States and Canada: A Research Synthesis," *American Journal of Public Health*, 89, No. 9 (1999): 1369–1376 at p. 1370.

²⁶³ N. M. Petry *et al.*, "Comorbidity of DSM-IV pathological Gambling and Other Psychiatric Disorders: Results from the National Epidemiologic Survey on Alcohol and Related Conditions," *Journal of Clinical Psychiatry*, 66, No. 5 (2005): 564–574 at p. 564.

²⁶⁴ As noted in a June 10, 2009 interview with Howard Shaffer, Director of the Division on Addictions and Associate Professor of Psychology in the Department of Psychiatry at the Cambridge Health Alliance.

gambling.²⁶⁵ In addition, commentators have suggested that the increased accessibility inherent in online gambling magnifies such risks.²⁶⁶ However, more recent studies specific to online gambling, most conducted since the advent of legal and regulated online gambling, have indicated that online gambling does not inherently encourage excessive gambling.²⁶⁷ For example, researchers at Harvard Medical School studied real-time betting activities of 48,000 Internet players over two years and found that their betting levels in Internet sports gambling and casino games were moderate. Most gamblers placed fewer than four bets per day, and sports gamblers tended to moderate their play based on their wins and losses; i.e., they played less often when they lost money and more often when they won money.²⁶⁸ Also, a large-scale British study in 2007 found no increase in the rate of problem gambling in the United Kingdom since 1999, despite a large increase in the number of new gambling opportunities (although the number of people who had gambled in the past year decreased between 1999 and 2007).²⁶⁹

C. Potential Effects of Legalization of Online Gambling on Problem Gambling

Some researchers and policymakers have expressed concerns about the impact of online gambling on problem gambling.²⁷⁰ They fear that legalization of online gambling might spur excessive gambling and problem gambling incidence by facilitating (1) unlimited access and availability of gambling platforms; (2) anonymity, which would allow gamblers to participate without fear of stigma; (3) gambling under the influence; (4) decreased perception of value of

²⁶⁵ See Brian Rush *et al.*, "Mapping the Prevalence of Problem Gambling and Its Association with Treatment Accessibility and Proximity to Gambling Venues," *Journal of Gambling Issues*, 20 (2007): 193–214.

²⁶⁶ As noted in interviews with Howard Shaffer, Director of the Division on Addictions and Associate Professor of Psychology in the Department of Psychiatry at the Cambridge Health Alliance, and Simon Holliday, Director of H2 Gambling Capital (U.K.).

²⁶⁷ Richard LaBrie *et al.*, "Assessing the Playing Field: A Prospective Longitudinal Study of Internet Sports Gambling Behavior," *Journal of Gambling Studies*, 23, No. 3 (2007): 231–243. Also see Richard LaBrie *et al.*, "Inside the Virtual Casino: A Prospective Longitudinal Study of Actual Internet Casino Gambling," *European Journal of Public Health*, 18, No. 4 (2008): 410–416. Also see Debi LaPlante *et al.*, "Sitting at the Virtual Poker Table: A Prospective Epidemiological Study of Actual Internet Poker Gambling Behavior," *Computers in Human Behavior*, 25, No. 3 (2009): 711–717.

²⁶⁸ See "Real-Time Betting Analysis of Internet Casino Gambling," *Responsible Gaming Quarterly*, 6, No. 2 (Fall 2008), at p. 9, http://www.americangaming.org/assets/files/RGQ_Fall_08.pdf (last accessed on August 10, 2009). Also, as noted in interviews with Peter Collins, Professor of Public Policy Studies and Director of the Center for the Study of Gambling at the University of Salford (U.K.), Bo Bernhard, Director of Gambling Research at the UNLV College of Hotel Administration, and Charles Wellford, Professor of Criminology and Criminal Justice at the University of Maryland, College Park, the availability of new forms of gambling does not necessarily lead to increased incidence of problem gambling.

²⁶⁹ See *Supra* at footnote 13, Heather Wardle *et al.* at p. 9–10.

²⁷⁰ Martin Owens and Guy C. Clark, "Internet Gambling Deserves a New Chance," *The Debate Room, Businessweek*, 2007, http://www.businessweek.com/debateroom/archives/2007/09/internet_gambli.html (last accessed on September 10, 2009). Also see Michael P. Scharf and Melanie K. Corrin, "On Dangerous Ground: Passive Personality Jurisdiction and the Prohibition of Internet Gambling," *New England Journal of International and Comparative Law*, 8, No. 1 (2002).

money; and (5) isolation.²⁷¹ A notable example of this concern is the 1999 assertion by the National Gambling Impact Study Commission that the three main reasons to prohibit online gambling are abuse by underage gamblers, addiction by pathological gamblers due to its high speed and instant gratification, and the potential for criminal activities.²⁷² Policymakers are also concerned about negative spillovers to the rest of society, including increases in crime, lost work and school hours, and increase in personal debt. However, the only reason cited in the Safe Port Act (the sponsoring legislation of the UIGEA) for banning financial transactions to and from online gambling sites is that it leads to debt collection problems for U.S. financial institutions.²⁷³

The following sections describe and analyze mechanisms through which legalization could affect the level of problem gambling in the United States. We identify several mechanisms by which legalization is commonly expected to increase the incidence of problem gambling and two mechanisms by which regulation might be expected to alleviate problem gambling.

1. Potential Adverse Effects of Legalization

The following section describes several mechanisms by which legalization is commonly expected to increase the incidence of problem gambling.

a. Removal of Legal Deterrence

Potential Effect: It is commonly believed that current legal restrictions on online gambling have deterred would-be gamblers from engaging in the Internet's version of gambling. Therefore, legalization may accentuate problem gambling by eliminating any legal inhibitions would-be gamblers have toward online gambling. In the 2007 UNLV survey of Nevadans, researchers found that approximately 12% of "non-online gamblers" (defined as those respondents who had not gambled online, but who may or may not have otherwise gambled) would be more likely to participate in online gambling if it were licensed and regulated by the state of Nevada.²⁷⁴

²⁷¹ See *Id* Scharf and Corrin. Also see *Supra* at footnote 25 at p. 50. Also Griffiths notes that among other factors, increased access to gambling provided by online gambling might facilitate the development of gambling related issues. M. D. Griffiths, "Internet Gambling: Issues, Concerns and Recommendations," *Cyberpsychology & Behavior*, 6, No. 6 (2003): 557-568; cited by Sarah E. Nelson *et al.*, "Real Limits in the Virtual World: Self-Limiting Behavior of Internet Gamblers," *Journal of Gambling Studies*, 24 (2008): 463-477, DOI 10.1007/s10899-008-9106-8. Also The Committee on the Social and Economic Impact of Pathological Gambling notes that "More people are gambling, and they are wagering more. As a result, there is increased concern about pathological gambling." The Committee further notes that "With the increased availability of gambling and new gambling technologies, pathological gambling has the potential to become even more widespread." National Research Council, *Pathological Gambling: A Critical Review* (National Academy Press, Washington, DC, 2005), at p. 3.

²⁷² *National Gambling Impact Study Commission, Final Report*, 1999, at p. 5-4 to 5-6, <http://govinfo.library.unt.edu/ngisc/reports/finrpt.html> (last accessed on September 10, 2009).

²⁷³ See *Supra* at footnote 69 at p. 62.

²⁷⁴ See *Supra* at footnote 6 Bo Bernhard at p. 25, 46. Note *N* = 1,000. Also 96.3% of responders were non-online gamblers; that is, they stated that they had not gambled online in the last five years.

Mitigating Considerations: It can be argued that the lifting of the prohibition itself is unlikely to have any significant impact on would-be gamblers' willingness to gamble online, because gamblers in the United States are generally ignorant or completely confused about existing legal restrictions.²⁷⁵ Support for this argument is found in the survey mentioned above, in which researchers discovered that 53.7% of responders were unclear regarding the legal status of online gambling. Approximately 17% thought online gambling was legal, and the remaining 29.5% thought it was illegal.²⁷⁶ This result indicates general confusion among gamblers in the United States about current legal restrictions.²⁷⁷ In addition, 87.9% of the responders noted that the current legal status of online gambling did not affect their desire to gamble online, whereas 4% indicated that their desire to gamble online was very much affected by its current legal status.

Moreover, the absence of any enforcement against online gamblers until very recently may have diluted the deterrent effect of legal restrictions on would-be gamblers' inclination to gamble, leading one to argue that complete removal of such restrictions in the future would not have a major impact on the behavior of would-be gamblers.²⁷⁸

b. *Introduction of Trustworthy Brands*

Potential Effect: Legalization may lead to increased comfort with gambling online, because U.S.-based sites, with trusted brands and subject to strict regulation, would offer a range of protections to gamblers that many offshore sites do not.²⁷⁹ Moreover, greater competition in the sector, with gambling platforms offering better deals to would-be gamblers, might lead to increased volumes and greater incidence of problem gambling.

Researchers indicate that security concerns and legitimacy are two main reasons cited by gamblers for not gambling online.²⁸⁰ Currently, Online Casino City, a guide to online gambling websites, lists 1,906 gambling websites from 70 different jurisdictions, 42 of which have sites

²⁷⁵ As noted in a June 5, 2009 interview with Keith Whyte, Executive Director of the National Council on Problem Gambling, Americans are generally ignorant of the legal status of online gambling, and many do not believe they will be prosecuted for gambling online.

²⁷⁶ Researchers further noted that 54% of non-online gamblers were unclear about the current status of online gambling, whereas 16% deemed it legal and the remaining 29% deemed it illegal. ²⁷⁶ See *Supra* at footnote 6 Bo Bernhard at p. 26.

²⁷⁷ Gaul notes that "even as bettors around the world gamble millions of dollars online, confusion reigns about the legal status of those bets and the companies that handle them." See *Supra* at footnote 83. Also, in a June 10, 2009 interview, Bo Bernhard, Director of Gambling Research at the UNLV College of Hotel Administration noted that the legal status of online gambling is "very unclear" in people's minds in the United States.

²⁷⁸ See *Supra* at footnote 14.

²⁷⁹ Section 2b discusses responsible gambling practices and safeguards that may be offered by regulated online gambling websites.

²⁸⁰ See *Supra* at footnote 19, Sally Monaghan.

that allow players from the United States.²⁸¹ The majority of these websites are privately owned, and many are located in countries with no reporting requirements.²⁸²

In such situations, where consumers are uncertain and have limited experiences with providers, brand associations are known to be particularly influential.²⁸³ In a recent survey, researchers at the University of Lethbridge found that the general reputation of the website was the most common reason identified by online gamblers for choosing to gamble at one Internet site over another.²⁸⁴ Thus, the introduction of branded providers that are inherently perceived to be trustworthy might attract more gamblers to participate in online gambling.²⁸⁵

Mitigating Considerations: It can be argued that gamblers most likely to be influenced by the availability of trusted brand-name sites are those who gamble already, perhaps in the casino environment, and hence know the brands.²⁸⁶ Although these gamblers may indeed shift their business, this shift would represent displacement, not overall growth. Further, the displacement would be from bricks-and-mortar to online gambling, which can offer more options and protections for problem gamblers than can land-based casinos.²⁸⁷

²⁸¹ As of September 14, 2009. See Online Casino City, *Online Gaming Site Owners*, <http://online.casinocity.com/ownership>. Also note, amongst these 1,906 sites are included 34 sites based in the United States, most of which involve skill games, free poker tournaments in which players can win real money, or state-sponsored lottery or sports betting.

²⁸² Gaul notes that in a joint investigation, the *Washington Post* and CBS's *60 Minutes* found that "many Internet gambling sites operate in a shadowy world of little regulation and even less enforcement," See *Supra* at footnote 83.

²⁸³ Stevie Watson *et al.*, "The Legalization of Internet Gambling: A Consumer Protection Perspective," *Journal of Public Policy & Marketing*, 23, No. 2 (2004): 209-213, at p. 211.

²⁸⁴ Robert Wood and Robert Williams conducted two surveys. The first survey was a random digit dial telephone survey of 8,498 Canadian adults conducted from January 2006 to June 2007. The second survey was an online self-administered survey of 12,521 adults from 105 countries, conducted from June to December 2007. See Robert Wood and Robert Williams, *Internet Gambling in Comparative Perspective: Patterns, Problems, and Interventions*, University of Lethbridge, Presentation to the Alberta Gambling Research Institute Annual Conference, March 2009.

²⁸⁵ As noted in an August 4, 2009 interview with Simon Holliday, Director of H2 Gambling Capital (U.K.), the legalization of online gambling would probably increase the number of online gamblers. Also, the previously cited UNLV study revealed that 12% of non-online gamblers would be more likely to participate in online gambling if it were licensed and regulated by Nevada. Although some of these respondents may fear legal repercussions, some may be unwilling to gamble online due to a lack of credible, branded providers, because a large portion of respondents had doubts about the integrity of online gambling. See *Supra* at footnote 73.

²⁸⁶ MGM Mirage, a large U.S. bricks-and-mortar casino operator, set up an Internet gambling site based in the Isle of Man and marketed the site using MGM's brand name and credibility. See Richard McGowan, *The Gambling Debate* (Westport, CT: Greenwood Press, 2008), at p. 43.

²⁸⁷ Wiebe and Lipton note that "If players value such regulation, then the unregulated operators will be at a competitive disadvantage." Jamie Wiebe and Michael Lipton, *An Overview of Internet Gambling Regulations*, submitted to the Ontario Problem Gambling Research Centre, August 2008, at p. 15.

c. *Increased Accessibility*

Potential Effect: One of the most common critiques of online gambling is the increase in access and availability inherent in Internet-based gambling platforms.²⁸⁸ Many believe that increased access to gambling and 24-hour-a-day availability may exacerbate problem gambling.²⁸⁹ In addition, online gambling also facilitates (1) anonymity, allowing gamblers to participate without fear of stigma; (2) gambling under the influence; and (3) decreased perception of the value of money, thereby elevating the risks of problem gambling. Potential risks posed by the frequency and speed of gaming, variety of games, and smaller permissible bet size on the Internet are frequently cited.²⁹⁰

Mitigating Considerations: U.S. residents already have online gambling options available to them all day, everyday, and from anywhere. So the addition of U.S.-licensed sites would not alter that particular reality.²⁹¹ Furthermore, as discussed in Section 2b below, regulation can assuage these concerns. Responsible gaming features and safeguards, including links to problem gambling help-lines and websites, self-exclusion programs, and self-imposed time and money limits, are some common features that can be enforced to curb problem gambling. In fact, some have suggested that problem gamblers may benefit the most from the legalization of online gambling, because they would gain access to the tools required by the regulator.²⁹²

d. *Easier Flow of Funds if UIGEA Restrictions are Lifted*

Potential Effect: Absent UIGEA restriction, U.S. residents would be able to make deposits to and withdrawals from online sites with greater ease. The UIGEA was intended to stop the transfer of funds from U.S. gamblers to online gambling websites. Instead of criminalizing gambling itself, the UIGEA was intended to prevent U.S. residents from gambling by restricting the role of financial institutions in transmitting payments to and from gaming operators.

Mitigating Considerations: Currently, enough workarounds have been designed, and are actively promoted to consumers by offshore online gambling sites, to render the existing restrictions largely ineffective. U.S. gamblers primarily use services provided by offshore financial intermediaries unrelated to gambling sites, such as e-wallets, that allow customers to get around the restrictions placed by the UIGEA. An e-wallet is an online account in which money can be deposited and used in commercial transactions. The e-wallet draws on a consumer's bank or

²⁸⁸ See *Supra* at footnote 69 at p. 61. Also noted in August 7, 2009 interview with Jamie Wiebe, Director at the Centre for the Advancement of Best Practices of the Ontario Responsible Gambling Council.

²⁸⁹ Michael Smeaton and Mark Griffiths, "Internet Gambling and Social Responsibility: An Exploratory Study," *CyberPsychology & Behavior*, 7, No. 1 (2004): 49-57, at p. 50.

²⁹⁰ See *Supra* at footnote 69 at p. 61.

²⁹¹ See *Supra* at footnote 153 at p. 15.

²⁹² As noted in an August 27, 2009 interview with André Wilsenach, Chief Executive Officer of the Alderney Gambling Control Commission.

credit card and routes the funds to the merchant, in this case an online gambling website. The most widely used e-wallets facilitate billions of dollars in commerce annually and are based and regulated offshore.²⁹³

The UIGEA restrictions have not produced the intended deterrence to online gambling and may have unintentionally led to the surfeit of unregulated offshore intermediaries, which act as alternatives to regulated U.S.-domiciled financial institutions. Removal of these restrictions is therefore expected to have limited impact on the incidence of problem gambling.

In addition, as discussed in Section E, legalization would give regulators an opportunity to gain better oversight on such international money transfers when routed through regulated financial institutions. It would also provide consumers with the protections already available to credit card holders in the event of fraud, disputes, and complaints.

e. *Advertising*

Potential Effect: Currently, the U.S. Department of Justice (DOJ) has the authority to prohibit the advertising of illegal Internet gambling websites. In 2003, the DOJ issued letters to the National Association of Broadcasters and other media groups noting that allowing advertising for online gambling websites may be considered aiding or abetting illegal gambling operations.²⁹⁴ Legalization of online gambling may, however, facilitate resumption of advertising in support of the online business.²⁹⁵

The high level of exposure to land- and river-based gambling and state lottery advertisements has contributed to gambling's normalization and perception as an ordinary and harmless activity.²⁹⁶ Various marketing strategies, including pop-up promotions, free or practice games, and direct email campaigns, are already being used to promote online gambling.²⁹⁷ Some advocates suggest that such advertising could lure would-be and existing gamblers to participate in online gambling, thereby leading to greater incidence of problem gambling.²⁹⁸

²⁹³ Todd notes that the UIGEA does not seem to have had an impact on online gambling in the United States. Aaron Todd, *NETeller Exit Impacts U.S. Internet Gambling Market*, onlineCasinoCity, Jan. 18, 2007, <http://online.casinocity.com/news/news.cfm?ArticleId=70015> (last accessed on September 11, 2009); cited by Gerd Alexander, "The U.S. on Tilt: Why the Unlawful Internet Gambling Enforcement Act is a Bad Bet," *Duke Law & Technology Review*, 5 (2008), at ¶6.

²⁹⁴ See *Supra* at footnote 60 at ¶11–12.

²⁹⁵ It should be noted, however, that the FTC and the various state attorneys general would in all likelihood retain jurisdiction over advertising online and the FCC would retain jurisdiction over advertising on broadcast and cable media.

²⁹⁶ See *Supra* at footnote 19 Sally Monaghan.

²⁹⁷ See *Id.*

²⁹⁸ See *Id.*

Mitigating Considerations: A note of caution is needed about the links that connect increased advertising for online gambling with increased problem gambling. First, the connection between increased advertising and aggregate growth of online gambling volume is likely and is supported by forecasts of increased online gambling post legalization.²⁹⁹ However, no research has been done to establish how much of the increase in online gambling is displacement of already existing land-based gambling versus new gamblers or increased activity by existing gamblers. Second, the connection between increased online gambling and increased incidence of problem gambling is also not established. Early research indicates that, at least in mature markets such as the United Kingdom, access to additional gambling opportunities in general and the addition of online gambling opportunities in particular do not appear to increase the incidence of problem gambling.³⁰⁰

Some regulations have been enacted to limit the advertisement of gambling products across various jurisdictions. In the United Kingdom, the introduction of the Gambling Act brought new restrictions on gambling advertising and subjected it to regulation by the Department for Culture, Media and Sport (DCMS), the British Gambling Commission, and the Advertising Standards Agency, as well as its former regulatory bodies, the Broadcast Committee of Advertising Practice (BCAP) and the Committee of Advertising Practice (CAP).³⁰¹ The various regulations include provisions prohibiting advertising to minors or vulnerable adults, among others.

In addition to these rules, however, the gambling industry has issued a “voluntary” code for socially responsible advertising, which specifically requires that advertisements include the address of the United Kingdom’s problem gambling help website and encourages operators to include responsible gambling messages in their advertisements.³⁰² The code also introduces a “watershed” time of 9 p.m., before which any newly permitted forms of gambling cannot be advertised, although the code does allow for the advertising of sports betting around televised

²⁹⁹ As noted in an August 4, 2009 interview with Simon Holliday, Director of H2 Gambling Capital (U.K.). Also, in a note to investors, the investment bank Goldman Sachs predicted a legalized online gambling market in the U.S. worth \$12 billion (more than double the estimated size of the current market). See Jon Parker, “US to legalize online gambling; worth \$12bn, Goldman Sachs predicts,” *eGaming Review*, June 29, 2009, <http://www.egrmagazine.com/news/industry/168682/us-to-legalise-online-gambling-worth-and3612bn-goldman-sachs-predicts.html> (last accessed on August 26, 2009). Also, in an analysis provided to a payment processing firm, PricewaterhouseCoopers estimated the federal revenue effect of legalized online gambling to range from \$13.0 billion (with a higher number of states opting out of the legislation) to \$25.9 billion (with a lower number of states opting out) for the period 2010–2019. See PricewaterhouseCoopers, *Estimate of Federal Revenue Effect of Proposal to Regulate and Tax Online Gambling – Executive Summary*, prepared for UC Group, April 24, 2009, <http://www.safeandsecureig.org/media/pwc09.pdf> (last accessed on August 28, 2009).

³⁰⁰ See *Supra* at footnote 293.

³⁰¹ Simon Fielder and Dominic Hodgkinson, *United Kingdom's Gambling Industry Adopts Voluntary Code on Advertising Standards*, Pillsbury Winthrop Shaw Pittman LLP, September 2007, <http://www.pillsburylaw.com/siteFiles/Publications/AD40F0C315922BF5A969E8BF6379B2E4.pdf> (last accessed on August 7, 2009).

³⁰² See *Id.*

sporting events.³⁰³ In Australia, advertising restrictions are determined by the states/territories; most prohibit advertising to minors and the use of misleading statements, while some have no specific regulations.³⁰⁴ The National Gaming Board of South Africa has set forth guidelines regarding advertising, prohibiting, among others, advertising to minors and advertising that may encourage excessive gambling.³⁰⁵ The U.S. could impose whatever targeted restrictions on advertising deemed necessary or appropriate.

2. Potential Benefits of Legalization

The following sections describe two mechanisms through which regulation could reduce problem gambling. Regulators could implement (1) public policy measures designed to educate the public on the dangers of problem gambling and (2) efforts to provide resources to those affected by problem gambling.³⁰⁶

a. *Access to Funding to Increase Awareness of Problem Gambling*

If the United States decides to legalize and tax online gambling, significant revenues may accrue from the imposition of taxes and license fees.³⁰⁷ Australia, Costa Rica, Great Britain, Aruba, and Antigua are some of the many countries that have recognized tax benefits from legalizing online gambling.³⁰⁸

The United States could use tax and license revenues to substantially boost publicly funded prevention, counseling, and treatment programs as well as research on gambling addiction.³⁰⁹ Currently, statutes in some states require that information regarding problem gambling be provided to persons participating in any form of legalized gambling. At least three states require that telephone helplines be maintained for problem gamblers.

³⁰³ See *Id.*

³⁰⁴ See Advertising Federation of Australia, *Gambling*, <http://www.afa.org.au/public/content/ViewCategory.aspx?id=509> (last accessed on August 7, 2009).

³⁰⁵ Mpande Advisors, *Report on the Regulation of Interactive Gambling*, prepared for the National Gambling Board of South Africa, October 2005, at p. 50 and 67.

³⁰⁶ See *Supra* at footnote 153. Also see *Supra* at footnote 60 at ¶11–12.

³⁰⁷ Researchers have estimated that at a flat tax rate of 6.25%, online gambling could generate more than \$750 million annually. See *Supra* at footnote 69 Christopher Grohman at p. 68.

³⁰⁸ See *Id.*

³⁰⁹ See *Supra* at footnote 258 Michael Belletire at p. 12–13. Also see General Accounting Office, *Internet Gambling: An overview of the Issues*, GAO-03-89, December 2002; cited by Gerd Alexander, “The U.S. on Tilt: Why the Unlawful Internet Gambling Enforcement Act is a Bad Bet,” *Duke Law & Technology Review*, 5 (2008), at ¶9.

Advocates for problem gamblers have been very vocal about the under-funding in existing budgets for prevention, counseling, and treatment services and observe that most health insurers currently do not cover these services.³¹⁰ Only 25 states provide any funding for problem gambling programs.³¹¹ Availability of tax dollars from online gambling revenues and licensing fees could be used to substantially bolster problem-gambling awareness and treatment programs, and to provide educational supports for parents and higher-educational institutions dealing with underage gambling.

b. *Wider Implementation of Responsible Gambling Features*

Legalization of online gambling could lead to the introduction and wider implementation of regulations that give online gamblers tools for controlling their own gambling behaviors.³¹²

Online gamblers today have access to a variety of online gambling options. However, research indicates the general lack of responsible gambling practices and safeguards offered by these online gambling websites. A 2004 exploratory study of 30 U.K.-based Internet gambling sites found that very few sites engaged in socially responsible practices.³¹³ Of the 30 sites, 26 had no reference to a problem gambling help resource; further, 20 sites showed no evidence of social responsibility and 29 sites did not seem to give an option to self-exclude from the site.

Various types of responsible gambling practices have been advocated, including links to problem gambling helplines and websites, self-exclusion programs, and self-imposed time and money limits.³¹⁴ Some common elements of regulatory structures across leading online gambling jurisdictions include (1) requiring operators to provide players with mechanisms to set their own

³¹⁰ Franklin discusses lack of federal funding for treatment or awareness of problem gambling, lack of insurance parity for problem gamblers, and limited or lack of funding from most states in the United States. Joanna Franklin, *Problem Gambling in the U.S – From the Beginning into 2001*. Presentation available at Responsible Gambling Council, http://www.responsiblegambling.org/articles/Problem_and_Pathological_Gambling_A_view_from_the_States.pdf (last accessed on September 10, 2009). Also Winslow discusses the lack of state funding for problem gambling services in Colorado and other states in the United States. Kyle Winslow, "A Problem for Gamblers," *The American Prospect*, March 10, 2008, http://www.prospect.org/cs/articles?article=a_problem_for_gamblers (last accessed on September 10, 2009).

³¹¹ As noted in a June 5, 2009 interview with Keith Whyte, Executive Director of the National Council on Problem Gambling.

³¹² See *Supra* at footnote 153 at p. 15.

³¹³ See *Supra* at footnote 25.

³¹⁴ As noted in a June 10, 2009 interview with Howard Shaffer, Director of the Division on Addictions and Associate Professor of Psychology in the Department of Psychiatry at the Cambridge Health Alliance. Also, as noted in a June 10, 2009 interview with Bo Bernhard, Director of Gambling Research at the UNLV College of Hotel Administration, Nova Scotia recently introduced voluntary loss limits as a self-regulatory device in its land-based gaming operations. Also as noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority, gambling websites regulated by Gibraltar have responsible gaming features such as "cool-off" periods and self-exclusions mechanisms.

betting limits or limit the deposits they make to their online gambling accounts; (2) requiring site operators to allow gamblers to self-exclude from participating in gambling with the operator; (3) permitting family members to petition to exclude a gambler from a website; (4) banning extension of credit to players; (5) requiring operators to display prominent links to support and counseling services.³¹⁵ In addition to these, the European Gaming and Betting Association lists approximately 50 provisions related to mitigating problem gambling.³¹⁶ U.S. regulators could use this list as a menu from which to identify and evaluate various safeguards. The list includes requiring registration pages to offer self-diagnostic tests designed to help would-be gamblers understand their own attitudes and vulnerabilities, and requiring operators to impose speed-of-play, compulsory time-outs, or player-loss-rate caps.³¹⁷ Aristotle, Inc., mentioned previously, has produced the Integrity Self-Exclusion List (SEL), an international database of people who have chosen to exclude themselves from bricks-and-mortar and online gambling.³¹⁸ If an excluded gambler attempts to open an account, Integrity will not return an approval code from its verification system.³¹⁹ Finally, gambling sites can train staff to identify spending patterns that indicate problem gambling and to contact the gambler directly.³²⁰

In assessing the general effectiveness of responsible gaming features in the context of online gambling, one 2008 study by researchers at Harvard University demonstrated that responsible gaming safeguards can be effective in the Internet gambling environment. With self-limits, online gamblers reduced their frequency of play—both the number of days on which they placed bets and the number of bets they placed per betting day. The amount they wagered per bet did not change significantly, although the online gamblers did reduce the total amount they wagered.

³²¹ In a large-scale survey of online gamblers, when asked about the usefulness of including

³¹⁵ See *Supra* at footnote 287 at p. 10–12. Also Grohman notes that the United States could set up a protocol such that banks or other financial institutions must monitor deposits onto sites and report habitual or problem gamblers to proper authorities. In addition, he notes that the government could empower families to monitor problem gamblers by installing monitoring chips in computers. See *Supra* at footnote 69 Christopher Grohman at p. 67. Also see *Supra* at footnote 25. Also see *Supra* at footnote 153 at p. 15. Also see *Australia: Uniform Standards for the Regulation of Interactive Gaming*, The National Working Party on Interactive Gaming, Exposure Draft, April 5, 2001, at p. 22.

³¹⁶ *EGBA Standards Benchmark Study: Overview*, European Gaming & Betting Association, 2008, Table 2, at p. 11–13.

³¹⁷ See *Id.*

³¹⁸ Integrity, *Self-Exclusion List (Online Gaming)*, Aristotle, Inc., http://integrity.aristotle.com/index2.php?option=com_content&do_pdf=1&id=52 (last accessed on August 11, 2009).

³¹⁹ See *Id.*

³²⁰ As noted in an August 5, 2009 interview with Phill Brear, Head of Gambling Regulation at the Gibraltar Regulatory Authority.

³²¹ Sarah E. Nelson *et al.*, “Real Limits in the Virtual World: Self-Limiting Behavior of Internet Gamblers,” *Journal of Gambling Studies*, 24 (2008): 463–477, <http://www.divisiononaddictions.org/html/reprints/selflimits.pdf> (last accessed on September 11, 2009), at p. 7.

responsible gambling features, such as self-imposed time limits, self-exclusion, regular financial statements, and regular self-assessments tests, online gamblers indicated that they would find it "quite useful." The Executive Director of the National Council on Problem Gambling, Keith Whyte, testified before the U.S. Congress as follows:

The graphical and interactive structure of the internet provides a revolutionary opportunity to create informed consumers with access to a variety of information designed to encourage safe choices and discourage unsafe behavior....

The technology also exists, unlike for other forms of gambling, to allow players and operators to set limits on time, wagers, deposits, etc...as well as to exclude themselves.³²²

D. Concluding Remarks

Legislative restrictions have failed to prevent U.S. gamblers from engaging in online gambling. Rather, those restrictions have led to additional business for Internet gambling operators beyond the regulatory reach of the United States. The current environment lacks responsible gaming features and safeguards offered to gamblers and limits publicly funded resources to educate the populace about problem gambling. We believe that regulators should be able to design sufficient protections to prevent any significant growth in problem gambling that results from legalization. Operators licensed within the United States should be required to offer a best-in-the-world range of services and resources for problem gamblers as well as to prevent underage gambling. Moreover, a proportion of the tax revenues and licensing fees derived from the U.S.-based industry could be used to substantially bolster the level of support for educational programs and services. According to André Wilsenach, head of the Alderney Gambling Control Commission, problem gamblers would receive "clear-cut" benefits from regulated online gambling, since land- and river-based gaming does not provide the tools that are possible in an online environment.³²³

³²² Statement of Keith Whyte, in U.S. House of Representatives, Committee on Financial Services, *Can Internet Gambling Be Effectively Regulated to Protect Consumers and the Payments System?* 110th Cong., 1st Session, June 8, 2007, at p. 120.

³²³ From an August 27, 2009 interview with André Wilsenach.

APPENDIX A

Table 1 provides an overview of the 10 risks, providing for each:

- an indication of protections afforded under the current U.S. regulatory framework;
- an indication of the natural regulatory structure and strategy for control; and
- comments regarding relevant technologies and tactics, and the respective role of other parties.

TABLE 1: Major Categories of Risk Related to Online Gambling

	<u>Category</u>	<u>Existing Protection</u>	<u>Natural Regulatory Structure & Strategy</u>	<u>Relevant Controls & Technologies</u>
1.	Gambling by minors	No effective protection. Offshore sites range from well regulated to completely unregulated.	Industry's short-run incentives: <i>supervisory</i> . Industry's long-run/strategic view: <i>cooperative</i> .	(Strongest form) Positive id matching at player registration against existing databases of known adults. Range of weaker forms of age verification available at player registration. Provision of child-protective software for parents, to keep minors off their parents' accounts.
2.	Consumers defrauded by site operators	No effective protection. Offshore sites range from well regulated to completely unregulated.	<i>Supervisory</i> : Enforcement focus aimed at disreputable operators. Exclusion of bad actors.	Vetting applicants and monitoring existing licensee behavior. Licensee oversight that includes software audits, mystery shopping, and betting pattern monitoring by regulator. Available complaint procedures: players report directly to regulators and have access to U.S. courts.
3.	Players cheated by other players	Detection mostly by other players. Remedies unavailable if sites deny the problem.	<i>Naturally cooperative</i> : Public and industry's interests both served by preserving integrity of games.	Comprehensive data retention by sites. Routine operation of pattern recognition systems for anomaly detection. Complaint procedures available for players to report anomalies to operators and to regulators. Regulatory oversight of complaint investigation and disposition.
4.	Involvement of organized crime	No effective protection with respect to offshore activities.	<i>Supervisory</i> : Enforcement focus aimed at disreputable operators. Exclusion of bad actors.	Vetting applicants and monitoring existing licensees/operators for <ul style="list-style-type: none"> • criminal backgrounds, • criminal associations, and • hidden ownership interests.
5.	Money laundering by site operators	Offshore operations subject to international cooperative enforcement efforts.	<i>Supervisory</i> : Enforcement focus aimed at disreputable operators. Exclusion of bad actors.	Vetting applicants and monitoring existing licensees/operators for <ul style="list-style-type: none"> • criminal backgrounds, • criminal associations, and • hidden ownership interests.
6.	Money laundering by players	No effective protection.	Short-run incentives: <i>supervisory</i> . Long-run/strategic view: <i>cooperative</i> .	Anti-money-laundering laws apply. Comprehensive data retention by sites. Details of every transaction recorded (not possible in casinos). Pattern recognition <ul style="list-style-type: none"> • by operators as part of a compliance operation, and • by regulators as part of oversight audit operation.

TABLE 1 (continued): Major Categories of Risk Related to Online Gambling

	Category	Existing Protection	Natural Regulatory Structure & Strategy	Relevant Controls & Technologies
7.	Violation of jurisdictional restrictions or prohibitions	No effective protection. States have no remedy with respect to offshore sites.	Short-run incentives: <i>supervisory</i> . Long-run/strategic view: <i>cooperative</i> .	Right of government to prohibit or restrict operators within state, and services offered to residents by operators outside of state. Federal regulation of licensees that obliges them to respect list of state exclusions/restrictions. Residence validation at player registration. Geolocation monitoring for each player session (e.g., by ISP analysis). Regulatory audits of operators' software controls. Mystery shopping/testing by states exercising rights to restrict. Federal and state remedy against licensed operators through federal or state law.
8.	Breaches of data confidentiality	No effective protection. Offshore operators outside U.S. jurisdiction.	Short-run incentives: <i>supervisory</i> . Long-run/strategic view: <i>cooperative</i> .	Licensees subject to all U.S.-based requirements regarding data confidentiality. Licensees subject to criminal sanctions and civil liability for breaches/abuses. Data-protection controls subject to audit.
9.	Communications and computer security failures	No effective protection. Offshore operators outside U.S. jurisdiction.	Short-run incentives: <i>supervisory</i> . Long-run/strategic view: <i>cooperative</i> .	Principal responsibility for state-of-the-art security should rest with site operators. Civil liability for site operators with respect to any harm to consumers. Regulator's role in auditing site security software/systems.
10.	Problem gambling behaviors	No effective protection. Offshore sites range from well regulated to completely unregulated.	Short-run incentives: <i>supervisory</i> . Long-run/strategic view: <i>cooperative</i> .	Site-imposed limitations & controls. Self-imposed exclusion options. Self-imposed limiting options. Taxes and license-fee revenue distribution can extend & enhance counseling & support services.

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Wood, Robert, and Robert Williams. *Internet Gambling in Comparative Perspective: Patterns, Problems, and Interventions*. University of Lethbridge. Presentation to the Alberta Gambling Research Institute Annual Conference, March 2009.

List of Individuals Interviewed

<u>Name</u>	<u>Date of Interview</u>
Parry Aftab Executive Director Wired Safety	05/27/2009
Bo Bernhard Director of Gambling Research UNLV College of Hotel Administration	06/10/2009
Michael Bolcerek Senior Vice-President of Business Development Aristotle	08/10/2009
Phill Brear Head of Gambling Regulation Gibraltar Regulatory Authority	08/05/2009
Peter Collins Professor of Public Policy Studies, Director of the Center for the Study of Gambling University of Salford (U.K.)	06/10/2009
Philip J. Cook Senior Associate Dean for Faculty and Research, ITT/ Terry Sanford Professor of Public Policy, Professor of Economics and Sociology Duke University	06/10/2009
Kelli Emerick Executive Director Secure ID Coalition	08/06/2009
Andrew Fritchie General Counsel PartyGaming PLC	08/21/2009
Glenn Gibson Manager, Technical and Systems Audit Tasmanian Gaming Commission (Australia)	08/05/2009

Damien Jarvis Assistant Director Liquor and Gaming Branch Tasmania Department of Treasury and Finance (Australia)	08/05/2009
Matthew Hill Director of Strategy, Research and Analysis British Gambling Commission (U.K.)	06/12/2009
Simon Holliday Director H2 Gambling Capital (U.K.)	08/04/2009
Joseph Kelly Professor SUNY Buffalo Business Law	06/01/2009
Paul Mathews Former Senior Vice President IGT Wagerworks	08/03/2009
Sam McQuade Graduate Program Coordinator College of Applied Science and Technology, Rochester Institute of Technology	06/03/2009
Katharina Riedl bwin (Austria)	08/13/2009
Paul Morris Policy Development Manager British Gambling Commission (U.K.)	06/12/2009
Chris Pinion National Account Manager LexisNexis Risk and Information Analytics	08/10/2009
Sue Schneider Founder Interactive Gaming News	08/17/2009
John Sealy Manager, Information Systems and Technology Services Licensing, Regulation and Alcohol Strategy Northern Territory Department of Justice (Australia)	08/31/2009

Howard Shaffer

06/10/2009

Director of Division on Addictions

Associate Professor of Psychology, Department of Psychiatry

The Cambridge Health Alliance, Harvard Medical School

Charles Wellford

06/17/2009

Professor of Criminology and Criminal Justice

University of Maryland, College Park

Keith S. Whyte

06/05/2009

Executive Director

National Council on Problem Gambling

Jamie Wiebe

08/07/2009

Director

Centre for the Advancement of Best Practices

Ontario Responsible Gambling Council (Canada)

André Wilsenach

08/27/2009

Chief Executive Officer

Alderney Gambling Control Commission

EXHIBIT B

Italy

5 Mar, 2010 / GamblingCompliance Ltd. / Francois Peglau

Italy has recently issued regulations to allow for the introduction of VLT machines, cash internet poker, new scratchcard lotteries and online casino games. In 2009 gaming companies operating in Italy collected €53bn in bets.

Recent Update

This report has been updated with the latest information on the implementation of online casino and cash poker games in Italy (see section 8.3 of the report). This report also contains information on the draft bill that is proposing the liberalisation of the land-based casino market (see section 9.1 of the report).

Furthermore, the report has been updated to include the latest news in the implementation of VLTs (see section 4.3.1) and on the new scratch lottery tender (see section 5.3 of the report). Also, information has been included on new money laundering regulation that has recently been enacted (section 13 of the report).

All statistics and charts have been updated to contain all 2009's gaming revenue data.

For convenience, all the substantive updates to this report have been highlighted.

1. Executive Summary

Until very recently, Italy's gaming market was closed to foreign competition. However, two landmark decisions issued by the European Court of Justice (Gambelli and Placanica) and the need for additional tax revenues drove the Italian government to gradually liberalise the gaming market. During 2006 the government issued more than 16,000 sport betting shops and betting corners licences by a tender process in which both local and foreign operators participated. In September 2008, the first legal remote tournament poker site was launched and now there are more than 50 sites online.

The opening of the market has generated a surge in gaming revenues. In 2009, Italian gaming operators collected more than €53bn in bets.

The Abruzzo earthquake that destroyed the medieval city of L'Aquila in April 2009 and the current global economic downturn have further encouraged the liberalisation trend. In the past year the Italian government has issued legislation that opens the market to the following activities:

1. VLT machines.
2. Remote cash poker.
3. Online fixed odds games of chance (casino games) and online bingo.
4. Four new licences for instant lottery (scratch lotteries) to be awarded through a public tender.

While in some cases (as remote cash poker and casino games) the government will need to enact secondary regulation before these games can be offered to the public, the developments that have unfolded over the last year have created new opportunities for foreign operators to participate in this much coveted market.

The government is also seeking to liberalise the land-based casino market and grant licences for 40 new casino venues in Italy. The draft bill proposing the liberalisation of this sector will be discussed in the Italian Cabinet in March 2009.

Another important development that should be taken in consideration is that the recent Bwin Liga decision issued by the European Court of Justice has implicitly validated the Italian online regulatory model; that is, the need to have a domestic licence even when operators are licenced in other EU Member State.

2. Historical Development Of Gambling

Gambling in Italy dates back to Roman times. Romans were fans of dice games and dice have been found in many Roman ruins. Romans even used small thin slabs of stone for gambling – these slabs being the precursors of card gambling.

Lottery games become very popular during the 16th century. The first lottery started in Genoa where the population could bet on five out of the 120 names of Genoese aristocrats who could be chosen as members of the governing Serenissimo Collegio. Lottery games gradually spread to other Italian cities and the draws began to be held every week instead of every year. During that time Italians started attending rooms known as "casini" to gamble. The word "casino" became synonymous of vice, especially in Venice.

In 1863, when Italy was unified, the State decided to take over most city lotteries to raise tax revenues and organised draw in the eight most important cities. In 1939, two more cities were added to the draws.

At the beginning of the 20th century casinos were run in semi-legal way. Several small casinos were scattered through the Italian territory and many were under the control of the mafia. After World War I, 58 casinos were closed as a result of a government crack-down. Mussolini slowly allowed the installation of a limited number of casinos (four of which continue operating today). The operation of slot machines was authorised in 1931. The same year criminal legislation was enacted in order to sanction illegal gambling. In particular, Royal Decree No. 773 of 18 June 1931 (Single Code of Legislation of Public Safety), prohibited operators not in possession of the necessary government or regulatory body licence or concession from offering betting, punishing any violations with a series of penalties. The prohibition was subsequently extended, in Law No. 401 of 13 December 1989, making it a criminal offense to operate unlicensed gambling by telephone or remote channels. Operators without an Italian licence were also penalised for advertising their services.

During the 20th century, the Italian gambling market was closely controlled by the government and by domestic companies. Until changes to legislation in 2004, the Italian gambling market was broadly split in four areas:

- The National Lottery (Consortio Lotterie Nazionali), managed by a monopolistic consortia.
- Licensed betting shop, racetracks and casinos.
- Gaming machines
- Illegal gambling operators or games operated in grey areas.

2.1 Market Liberalisation

During the 1990s and first years of the 21st century, many foreign operators tried to break into the Italian market. The Italian government and the national lottery have tried to defend their territory, especially the position of the lottery monopoly that provides important revenues to the national budget. In the late 90s Italian authorities started prosecuting foreign operators (such as Stanley International) and the agents that were working in their behalf in Italy. One of the most famous cases related to a number of Stanley's betting agents and was finally decided by the European Court of Justice (ECJ). In the Gambelli decision the court clearly stated that economic motives were not valid reasons to defend a gambling monopoly in the EU. While initially Gambelli was considered a victory for foreign bookmakers, Italian courts later validated the lottery monopoly, maintaining the status quo.

However, the ECJ delivered a further blow to the Italian model with the Placanica decision, which established that many of the protectionist measures implemented by Italy to defend its market were against EU regulation. The Gambelli and Placanica decisions generated a change in Italy's policies toward gambling as they showed that the attempts to defend the monopoly could run foul of EU law and Italy could risk 'a back door liberalisation' as more cases were pushed up to the ECJ and the EC Commissioner. In that sense, Italy decided to gradually open the market under its own conditions. The Italian government current position with regards to gaming can be summarized in the following recent comments given by Francesco Rodano, Head of the Remote Gaming Department at AAMS:

*"We [Italy] represent a sort of balanced third way between strict monopolies and completely open systems. Let's say that we are in a 'regulated liberalisation' scenario. Our strong principle is: if you want to collect money from the Italian citizens you must have an Italian licence and operate under our rules"*¹

In 2004 the first important reform in Italian market took place and was directed at the slot machine market. Up to that date, the Comma 6 machines (AWP style machine) market was not closely controlled by the government, therefore there was a significant number of illegal machines operating. Legislation introduced by the Amministrazione Autonoma Dei Monopoli Di Stato (AAMS) established that all Comma 6 machines had to be connected to the Ministry of Finance in real time. This measure removed a significant number of illegal machines from the market and allowed the government to control this highly profitable market.

An important step towards the opening of the market was the enactment of a 2005 betting shop licensing regime. A number of 'telematic' licences were granted that allowed a betting shop to be operated as a hub for network internet terminals in cafes and kiosks, legalising the existing business structure of the agent-network model. The licences issued in 2005 will be valid until 2011.

In 2006 a new betting licence regime was enacted (under the "Bersani Law") and a new tender process was organised. The 2006 tender process gave away 16,700 split in four parts:

- 2,300 sport betting shops.
- 4,400 sport betting 'corners'.²
- 500 horseracing shops.
- 9,500 horse racing 'corners'.

Also, remote licensing was extended to products given under the 2005 'telematic licence'.

The licences were auctioned in the last quarter of 2006 and 112 companies successfully bid for a licence. The Italian government made €430m with the tender process. While many foreign operators were able to obtain betting licences, the whole tender process was dominated by local companies such as SNAI and Matchpoint. SNAI was the overall winner of the tender process securing a total of 5,104 licences (3,898 horses and 1,206 sport) of the 16,700 licences whilst Match Point, the betting division of Lottery operator SISAL, came second with 3,134 horseracing outlets and 765 for sport, a total of 3,899. Lottomatica, a major Italian operator with terminals processing both gaming and non-gaming products in thousands of bars and tobacconists throughout the country, unsurprisingly bid strongly for corners, securing 1,137 for sport and 500 for horses. Seven successful bids for dedicated sports outlets brought its overall total to 1,194.

The only foreign companies to make their mark were the Greek company Intralot, which secured the largest number of new dedicated sports betting outlets in the country (416) as well as a further 164 sports corners and 9 horseracing betting shop, Coral Eurobet (403 licences in total) and Ladbrokes, who had acquired control of the Italian operator Pianetta Scommesse in the summer (142). Leisure & Gaming and a joint venture between William Hill and Codere also obtained a small number of licences.

2007 and 2008 saw further developments in Italian gaming market, most notably with the legalisation of internet game of skills such as tournament poker. The opening of this new business activity has provided a great boost to the market and to the government revenue collection (the Italian taxman takes 3 percent of every tournament fee). According to a report prepared by the Rome based consulting company TrustPartners srl, Italian poker market will be worth €2.5bn per year by 2012.

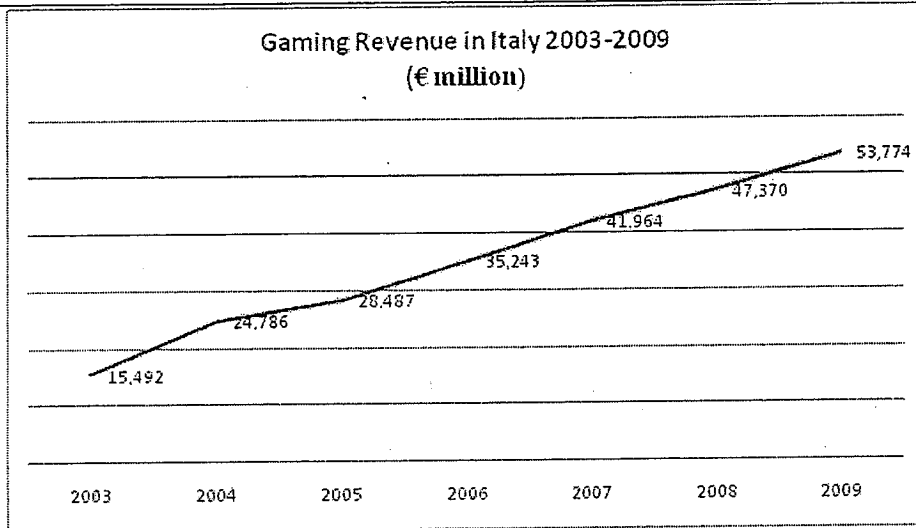
In 2009, the need for additional revenue to cover the reconstruction of the region of Abruzzo, destroyed by an earthquake in April 2009 drove the Italian government to accelerate the reform, opening the online market to cash poker, VLT machines and new online games such as bingo and casino games.

3. The Gaming Market Today

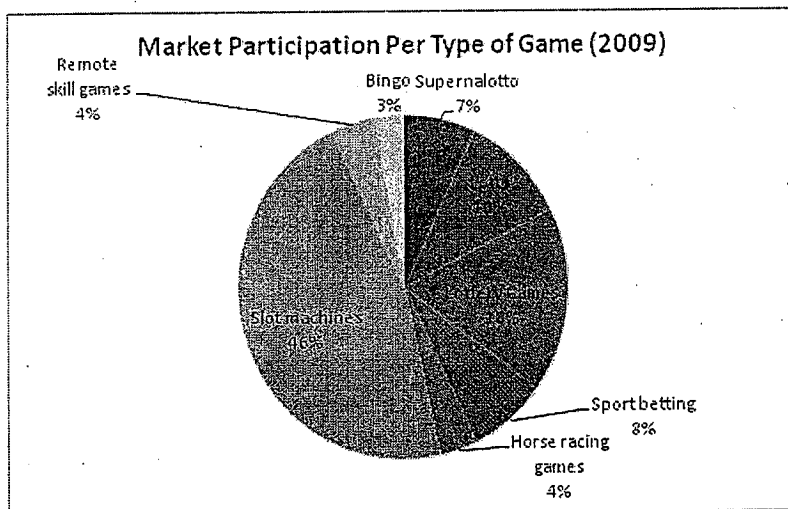
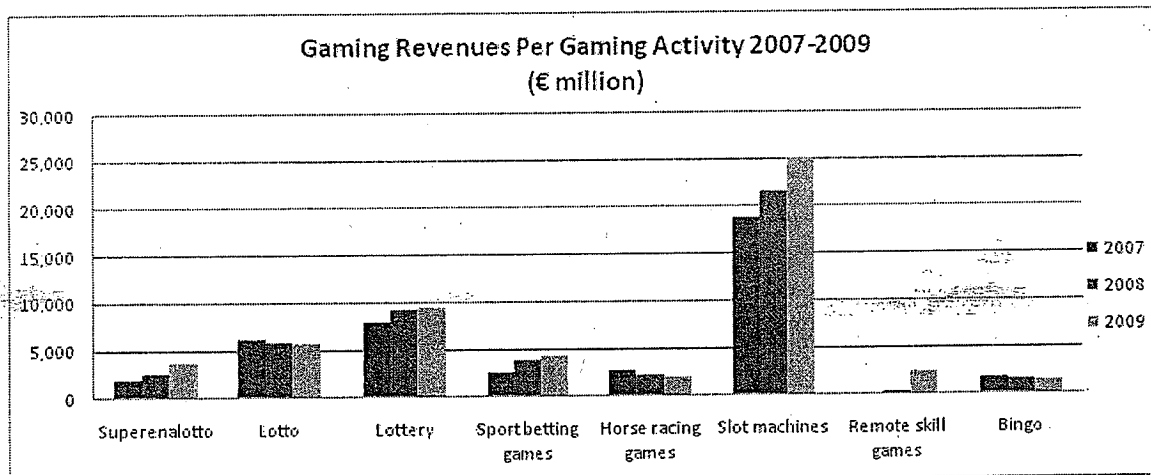
Italy's gambling industry is traditionally dominated by concession holders, which span the various sectors and innumerable retail and points of sale scattered around the country. In recent years, foreign operators wanting to break into this jurisdiction have utilised EU law, seeking the freedoms guaranteed in the EU Treaty through the freedom of establishment and the right to provide services.

Initially, the government position was to restrict the entrance of foreign operators and prosecute any operator offering gaming in Italy without a domestic licence. However, in the last years, after several legal defeats before the European Court of Justice, the Italian market has started gradually to open to new participants and new gaming activities as remote gaming.

According to preliminary reports issued by AAMS, gaming operators in Italy collected revenues for €53.7bn in 2009, a 13.52 percent increase from the amounts collected in 2008.



According to the AAMS, the following amounts were collected in Italy from the principal gaming activities during the period 2007-2009:



Source: AAMS

According to Agicoscommesse, the overall improvement in the Italian market in 2009 is due to the following factors:

- a) The stabilisation of lottery revenues mainly as a result of the success of the Gratta e Vinci (scratch lottery) managed by Consorzio Lotterie Nazionali.
- b) The continuous increase in the demand of slot machines gaming.
- c) A gradual reduction of gaming taxes in horse racing, sport betting, lottery games, Superenalotto and slot machines. The average rate in taxation has decreased from 22.6 percent in 2003 to 16.2 percent in 2008. Another important factor is that additional resources obtained from the decrease in taxation have been destined to fund better payouts levels for players (more than 69 percent of the collected revenue).
- d) The stabilisation and growth of the online market, which collected in 2009 more than €3.7bn.
- e) The modernisation of the commercialisation network for Superenalotto and SuperStar.

Some of the major concession holders in the Italian market are:

Lottomatica: One of the leading lottery operators in the world. The company is controlled by the De Agostini Group. Lottomatica has the monopoly over the Lotto game, as well as the instant and deferred lotteries (Gratta e Vinci) through a consortium (Consorzio Lotterie Nazionali - National Lottery Consortium). Lottomatica also operates AWP machines, sport betting games (the company obtained revenues of €70.3m in the first half of 2009) and internet skill games (in the first half of 2009, the company obtained revenues of €19.2m from €161.9m wagers).

Sisal S.p.A: The company operates lottery games (SuperEnalotto), sports betting games (Totip +, Tris, Totocalcio, Totogol, Big Match, amongst others), AWP machines and recently started operating online poker games. Sisal also manages a TV Channel (Sisal TV) which is completely dedicated to games of chance. Sisal controls Match Point the first Italian betting concessionaire which has a network of outlets throughout Italy for horse racing and sport betting.

SNAI: The company is one of the main providers in the design and implementation of products and services in the gambling sector and in its related services. SNAI is also one of the most prominent operators of sport betting and pool betting, bingo, AWP machines and recently online poker. SNAI also owns a horse track in Milan.

Intralot Italia: The Greek multinational established itself in Italy in December 2006 and is one of the most successful foreign operators in Italy. In 2007 it managed 416 sport outlets, 164 sports corners and 9 horse racing betting shops and currently also offers such products from an online platform. In 2008 Intralot bought the operation of Codere and William Hill in Italy adding 55 more outlets to its retail business. In April 2009, Intralot entered in a cooperation agreement with PartyGaming in order to launch its own online poker tournament service in Italy. In 2010 it has also entered into a partnership with Cogotech for the operation of the new VLT market.

Leisure & Gaming (Betshop): The group operates in Italy through the brand "Betshop". Up to 2008 they operated 52 betting outlets and a partner network totalling 584 venues mainly covering the centre and south of Italy. They also operate internet tournament poker games in Italy.

Cirsa: The Spanish gaming conglomerate manages 6,800 AWP machines in Italy.

Eurobet Italia (Gala Coral): The company obtained 403 licences for sports betting shops and horse races betting in the 2006 tender process and in 2007 started rolling out the venues. Eurobet is also offering online tournament poker.

We must also mention the case of **Stanley International Betting (Stanleybet)**, the Liverpool based operator. Stanleybet has not obtained an official concession in Italy but has a very strong presence in the market. Since the 1990s Stanleybet developed an extensive network of agents and data transmission centres that collect bets from Italian punters and process them in the UK. This modus operandi brought prosecution and lawsuits against Stanley's Italian agents that eventually lead the ECJ to issue the landmark Gambelli and Placanica decisions. Stanley continues collecting bets in Italy and has a number of pendant lawsuits that will be decided by Italian courts.

Another "unofficial" participant of the Italian market is the Punti di Commercializzazione (PDC). The PDCs, previously known as "Punti Remoti", are outlets that in theory provide support to Italian website operations.

On these premises punters are able to pay in cash to acquire prepaid cards for use on the sites, carry out registration, and use the internet. In theory, they are not legal betting shops but in reality many of the outlets are virtual betting shops where punters pay in cash and receive cash prizes paid by the owner of the PDC, competing directly with licence betting shops (which had to pay considerable amounts of money in order to obtain their concession).

While Italy is a highly coveted market for foreign operators, not many have been successful in breaking into it. The most problematic issues with this market have been the continued presence of illegal betting shops and the significant competition from established operators. Other operators have cited the complexities and complications required to adapt to the unique system that the regulator AAMS and technical partner SOGEI have insisted on imposing, as well as the bureaucratic hurdles that need to be surmounted in order to install a betting shop in Italy.

As a result of this, many foreign operators that initially entered the market with the liberalisation process, have decided to leave. For example, Codere and William Hill won a number of horse-racing and sports-betting concessions to operate in Italy back in December 2006. However, in 2008 both companies decided to sell their share of the business to Intralot as the number of licences they had in Italy was "insufficient in scale to provide an attractive long-term return".

Sportingbet, which had launched its Italian operation in May 2006 decided to sell this business in July 2009 after it failed to turn a profit in that time. Following in their footsteps, in August 2009 Ladbrokes announced that it was putting its loss-making Italian betting shops up for sale for an estimated £50 million. Ladbrokes had already made an impairment charge of £27.8m with regards to its Italian betting shop business. It is speculated that the business may be bought either by SNAI or Lottomatica, as well as the Greek owned Intralot Italia.

Despite these difficulties, the opening of the online market for tournament poker has attracted a new wave of foreign online operators that are trying to break this profitable but complicated market. New entrants are expected with the liberalisation of online casino games and cash poker in 2010 (see section 8).

3.1 Supervision

Over the past 20 years the responsibility for regulation of the gambling sector has been transferred to the Amministrazione Autonoma Dei Monopoli Di Stato ('AAMS' herein), the monopolies administrator.

AAMS was setup by Legislative Decree No. 2258 of December 8 1927, for the performance of "monopoly services involving the production, import, sale of salt and tobacco, as well as the production and sale of State-sponsored quinine".

During the 1980s and 1990s, in realisation of a strategy designed to rationalise different sectors, AAMS took over the management and regulation of national lotteries (1988), lotto and instant lotteries (1994), Bingo (2000) and SuperEnalotto (2002).

In 2002, Law No. 178 of August 8 2002 brought all State-run gambling activities, which the Ministry of Finance and Economy previously oversaw, to AAMS.

Similar to when the Ministry of Finance and Economy was the regulator, AAMS has the power to either run gambling activities directly, or it can transfer the right of operation to private or public sector bodies - through the grant of a licence or concession.

Furthermore, the law of 2002, also transferred to AAMS the powers to run sports linked gambling and betting, which were once assigned to the Olympic Committee (entity that in the past was on charge of gaming supervision).

Under the Finance Act 2008 a provision was introduced aimed at transforming AAMS into a more independent governmental agency.

AAMS has the regulatory responsibility over:

Games of chance

- Lotteries: Lotto, SuperEnalotto, deferred draws and instant lotteries, remote lotteries.
- Bingo and online bingo: which are offered exclusively on licensed premises, bingo halls by licensed operators.

- Online casino games and other games of chance (internet fixed odd games): These games will be introduced in summer 2010.

Betting

- Pools: which are run on sports events, horse racing and other events. These are offered to the public through a network of licensed retail outlets as well as online.
- Betting on horse races: through both totalisator and fixed- odds forms at licensed betting shops and on- course bookmakers, as well as online.
- Betting on sports and other events: through both totalisator and fixed- odds at locations such as licensed betting shops, lottery outlets and betting 'corners', as well as online.

Games of skill

- Tournament poker and cash poker (to be introduced in 2010).

Gaming machines:

- Comma 6 (AWPs also known as 'NewSlot'): which offer cash prizes up to a maximum of €100, and can be installed in licensed gaming houses, bingo halls and in appropriately designated commercial premises, which are linked to one another through remote networks and then all connected to a centralised system controlled by AAMS.
- Comma 7c (skills without pay machines- SWPs): also come under the regulation of AAMS, with these types of machines, needing to be installed on licensed premises.
- Comma 7a (video lottery machines - VLTs): this type of machine have been included in a past financial law, however, no such machines have been introduced up to 2008. Recently, new regulation has been enacted and these machines will be implemented in the summer of 2010.

AAMS regulates the lion's share of the Italian gambling sector. However, there are a number of areas of gambling that are still controlled by other authorities. These are:

- Casinos: run by local authorities (the provinces and municipalities) under the control of the Ministry of the Interior.
- Lotteries, bingo and tombola, where the total prize value does not exceed €51,645. Furthermore, these types of games have to be associated with local events. Local authorities and AAMS must also be notified.
- Promotional competitions involving prizes. These are controlled by the Ministry of Economic Development, with AAMS having some control and exercising supervisory powers that seek to protect the State's interest in the gambling sector.

3.2 Recent Important Regulatory Developments (Decreto Abruzzo, Legge Comunitaria 2008 And Decreto Anti- Crisi)

The region of Abruzzo was hit by a strong earthquake on April 6 2009, severely damaging the medieval city of L'Aquila and killing 307 people. The need for additional revenue to fund the €1bn bill for reconstructing the Abruzzo region has prompted the government to liberalise the Italian gambling market even further. In April, June and August 2009 the Italian government enacted three pieces of legislation that introduced important changes to the gaming legislative framework in Italy; Decreto Legge No. 39 of April 28 2009 (Decreto Abruzzo), (converted in Law 24 of June 2009, n. 77), Legge 7 de luglio 2009, 88 (Comunitaria 2008) and Decreto Legge No 78 of July 1 2009 (Decreto Anti- crisi, converted in Law 3 of August 2009, 102).

The commented regulation established regulatory framework for the introduction of online casino games, cash poker and VLT machines. This regulation also established the initial tender conditions for the new scratch lottery to be offered in 2010. The specific content of this regulation is summarised in Annex I of this report and it is also mentioned in the specific sectors where this legislation is relevant.

4. Slot Machines

Gaming machines have been in Italy for many decades, with the first pinball machine arriving on the market in the 1940s. Gaming machines were first regulated in 1965, when legislation came into force which sought to protect the inland revenue of the State. However, it was not until 2002 when the legislature decided to define what constituted a gaming machine and in the process introduced different categories depending on the goal of players (whether the game is for entertainment or a combination of entertainment, skill or monetary

reward). It was only recently when machines which fall into the 'slot' machine category have been introduced into Italy.

4.1 Statistics

Slot machine gaming continues to be the most important gaming activity in Italy. For 2009, slot machines represented 46.4 percent of the gaming market revenue.

Comma 6a/ NewSlot machines were introduced onto the Italian market in 2004 and their characteristics are similar to AWP's. Turnover for the NewSlot market in its first year (2004) was €8.679bn. For 2009 the turnover for slot machines had already increased to €25bn.

There were 186,000 machines registered in 2005, which increased to about 290,000 for 2006. Up to August 2009 there were more than 400,000 authorised slot machines in Italy. Italy slot machine market is dominated by local operators. The biggest operator is Atlantis World, which manages 85,376 slots. Other important players are Lottomatica, Gamenet and Cogotech.

Operator	Number of machines (August 2009)
Atlantis World	85,376
Lottomatica	76,867
Gamenet	55,752
Cogotech	37,329
SNAI	36,088
Sisal Slot	35,172
HBG Connex	34,270
Cirsa Italia	18,453
Gmatica	15,971
Codere	9,707
TOTAL	404,985

Source: AAMS

NewSlot machines are located in over 85,000 premises from coffee houses, to restaurants and arcades.

4.2 Legislative Framework

The most important regulation regarding slot machine is contained in the Royal Decree No. 773 of the 18 of June (TULPS- Public Security Act). Further specific regulations for gaming machines are as follows:

- Law No. 289 of December 27 2002: this law defines what measures are to be adopted to combat the illegal use of machines.
- Implementation Decree of March 11 2003: this decree defines technical requirements regarding machines which do not offer cash prizes.
- Implementation Decree of April 10 2003: this decree defines technical requirements regarding machines which do offer cash prizes.
- Implementation Decree of December 4 2003: this decree defines technical manufacturing and technical control requirements of machines which offer cash prizes.
- Implementation Decree of January 27 2004: this decree gives approval for a framework of agreement between AAMS and the inspection and certification bodies (mentioned above).
- Decree No. 86 of the Ministry of Finance of March 12 2004: this decree outlines and defines the functions of the online communications network for the management and linking up of NewSlot machines, with a gaming control which operates at a central level.
- Implementation Decree of July 1 2004: this decree outlines the granting of licences for the installation of NewSlot machines.
- Law No. 266 of December 23 2005 (the Financial Law of 2006): this law creates a new category of machine - Video Lottery Terminals (VLTs).
- The Joint- Directors' Decree of November 8 2005: this decree sets out technical requirements for machines which do not offer cash prizes.
- Implementation Decree of September 19 2006: this decree further amends the technical requirements for amusement machines, with the introduction of an electronic device which is controlled by AAMS, running on the machines file.
- Article 1 (Paragraphs 81 and 86) of Law No. 296 of December 27 2006 (the Financial Law 2007): this law outlines new regulations regarding tax liabilities, communication obligations, tax deadlines, and other accounting requirements and sanctions.
- Implementation Decree of January 18 2007: this decree outlines the maximum number of machines which can be installed in a retail outlet, including bingo clubs.
- Implementation Decree of December 4 2007: this decree deals with the fulfilment of tax payments and the rules concerning how licenceholders communicate their taxation liabilities.
- Decreto Abruzzo

4.3 Licensing

The installation and the use of both automatic and semi- automatic gaming machines (and particularly videopoker devices) is banned by Decree No. 773 of June 18 1931 (otherwise known as the TULPS - Public Security Act) in:

- Public places.
- Places open to the general public.
- Clubs or any kind of association.

An exception to this general prohibition is found in Article 110 (commas 5 and 6) of the TULPS Act, for machines which fall into the category of amusement machines - where the player's skill and the entertainment value of the machines play are of greater importance in the outcome of the game than mere chance.

The so called 'NewSlot' machines fall into this category. These machines were introduced after changes to the legislative framework (through the 2003 Budget law), with the first NewSlots launched in 2004. Some specifics about the NewSlot machines are:

- Winnings are in cash but cannot be more than €100 (an increase from €50).
- The minimum duration of a game is four seconds.
- The game can only start when a coin of maximum value €1 (an increase from €0.50) into the machine.
- Winnings are calculated by the machine, over a cycle of no more than 140,000 games (an increase from a game cycle of 14,000).

- The winnings cannot be less than 75 percent of the total amount bet.
- The machines cannot offer poker or games which are played in the same way as poker.
- People under the age of 18 cannot use the machines.
- Installation of these machines is only allowed in retail outlets, places which are open to the public, private clubs and authorised associations (in line with the requirements found in Articles 86 and 88 of the TULPS Act). These places include bars, restaurants, hotels, lido recreation facilities, coffee houses, amusement arcades, agencies and points-of-sale for horse race and sports betting and private clubs.
- The game must include elements of skill or entertainment in addition to the random element.

New Slots are so called 'chance- programmed' AWP machines where the percentage payout is fixed and regulated by a software algorithm that (through compensators) unpredictably distributes the winnings across a pre- defined game cycle, through sporadic wins or enriched winning periods.

Machines need certification as complying with the law and technical requirements published by AAMS and the Ministry of Internal Affairs. This certification needs to be by a company which is approved by AAMS to provide certificate of inspection. The following table (from AAMS's website) includes the most recent list of certification bodies approved by AAMS:

DENOMINAZIONE	INDIRIZZO	TELEFONO	FAX
APPLUS+ CTC (LGAI)	Campus de la UAB Apartado Correos, 18 08193 Bellaterra - Barcelona - SPAGNA	+34 93 5622000	+34 93 5622001
GLI Italy B.V. Filiale Italiana	Zona Roveri, 2 - Via Maestri del Lavoro, 3 40138 BOLOGNA (BO)	051 533660	051 534000
NMI CERTIN B.V.	Schoemakerstraat, 97 - Delft - OLANDA	+31 78 6332332	+31 78 6332309
	Sede Italiana Via Dandolo, 17/A - 35010 Borgoricco (PD)	049 9335925	049 9339698
QUINEL QUALITY IN ELECTRONICS	Feldstrasse, 6 - 6300 ZUGO - SVIZZERA	+41 417244227	+41 417243038
	Sede Italiana Via Bonni, 5 - Loc. Interporto - 43010 Fontevivo (PR)	0521 617328	0521 615279
SGS Italia S.p.A.	Via G. Gozzi, 1/A - 20129 MILANO (MI)	02 73931	02 70124630
SIQ	Trzaska cesta, 2 - Ljubana - SLOVENIA	+386 1 4778160	+386 1 4778444
	Sede Italiana Via Terza Armata, 181 - 34170 GORIZIA (GO)	0481 20950	0481 519019

In 2004 a dedicated online communications network was set up to control all the gambling operations of NewSlots - in part to combat illegal gambling. NewSlot machines can only operate if connected to a remote network controlled by AAMS. If interfered with, the machines are automatically blocked from the network. Furthermore, AAMS believes that this remote network (which claims is the only one in the world), represents the future for slot machines. AAMS guarantees it can monitor every single machine, checking that they are functioning properly, ensuring player protection and protection against interference and tampering with machines, while ensuring that concession holders are complying with their requirements.

Authorisations for private operators (including administrators, owners of gaming premises and licence holders of the online network) are granted by AAMS in line with technical requirements, along with requirements established by the Department of Security/ Public Safety in the Italian Ministry of Internal Affairs. In general, the following categories of operators need to possess a licence, granted in accordance with the TULPS Act, in order to be able to assign operational and distribution licences for NewSlots:

- Manufacturers
- Importers
- Distributors
- Those in management of the machines.

Machines which are not NewSlot machines and do not offer prize money, fall into a different category under the TULPS Act (Article 110, Paragraph 7(a) and 7(c), or Comma 7c machines). These types of machines generally use simpler technology, are well known and have been around for many years. Examples include pool, juke boxes, table football, pinball. These machines need to comply with the following requirements:

- Must test players' physical, mental or strategic skill.
- Prizes consist of small objects/ gadgets, with a value of no more than 20 times the cost of playing (with a maximum of €20).
- Prizes cannot be exchanged for cash.
- Free games are not permitted.
- No games of chance are allowed to be provided (including poker, blackjack, roulette etc.)

- Obscene or violent images are not allowed.
- Anti-tamper devices must be installed on each machine.
- Installation is only allowed in retail outlets, places which are open to the public, private clubs and authorised associations (in line with the requirements found in Articles 86 and 88 of the TULPS Act). Installation is also allowed in travelling theatre companies premises (in accordance with Article 69 of the TULPS Act).

4.3.1 Video Lotteries Terminals (VLT)

Law No. 266 of December 23 2005 (the Financial Law of 2006) introduced a new category of machine - Video Lottery Terminals (VLTs) devices. However, further regulation was needed before these machines could be installed. The Decreto Abruzzo in 2009 authorized the experimental introduction of VLTs and defined them as machines that are controlled remotely, that have a remote digital random generator of winning combinations and that provide payout for player equivalent to 85 percent of the played amounts (see point 3.2 of this report).

Operators will need to pay €15,000 for the installation of each machine. Existing operators will only be able to obtain VLT licences up to 14 percent of the number of AWP that they already operate.

In August, AAMS published Decree of the 6 of August of 2009 that regulates certain aspects for the installation of VLTs. This disposition established, amongst others, the following conditions:

1. VLTs will need to be interconnected with the communication network established by the AAMS. The implementation of VLTs to this network will need to be made before October 30, 2010.
2. After the AAMS publishes a public notice (probably before September 15 2009) the operators will have 15 days to tell the AAMS the number of machines they intend to install (without exceeding the 14 percent limit of the AWP machines they operate at the time of the publication of the Decreto Abruzzo). AAMS will verify the payment of the first instalment of the established fee and will check the compliance of the testing and machine requirements.
3. While existing slots operators will be able to install a number of machines equal to 14 percent of their existing estate of AWP – on payment to the government of a one-off fee of €15,000 – new operators will also be allowed to install machines should the total number of machines requested be less than 14 percent of the total number of slots in the market, which is presently around 275,000. These licences will be allocated through a tender process. The base value will be €15,000 for each VLT and the payment of this amount will be made in two instalments, payable in November 2009 and June 2010.
4. The regulations indicate that duty on the machines will be 2 percent of stakes in the period 2009-2011, rising thereafter to 3 percent in 2012 and 4 percent in 2013. The technical requirements applicable for the operation of VLTs are explained [here](#).

All the existing AWP operators took all the available 56,697 VLT licences, leaving no available licences to new operators. In that sense, the biggest VLT operator will be Atlantis World which secured 11,953 VLT licences. The only international operators able to obtain a licence were Cirsa and Codere. Intralot will also

benefit from the VLT market as Cogotech has signed a partnership with the Greek multinational in order to exploit jointly the VLT business in Intralot's betting shops.

Operator	Number of slot machines (August 2009)	Number of VLT licences obtained
Atlantis World	85,376	11,953
Lottomatica	76,867	10,761
Gamenet	55,752	7,805
Cogotech	37,329	5,226
SNAI	36,088	5,052
Sisal Slot	35,172	4,924
HBG Connex	34,270	4,798
Cirsa Italia	18,453	2,583
Gmatica	15,971	2,236
Codere	9,707	1,359
TOTAL	404,985	56,697

Source: AAMS

Manufacturers are also benefiting from the introduction of VLTs. Lottomatica's subsidiary Spielo has already closed a deal to provide VLTs to Gamenet in a deal estimated in €40- €45m. Astro Corps, already the largest supplier of AWP's in the Italian market, has confirmed a supply agreement with Codere for 450 VLT systems.

It is expected that the launch of VLT operations will start this summer. However, concerns grow over the competition from unlicensed computer terminals known as Totems. Totems are dedicated computer terminals used to gamble over the internet that are usually found within bars, cafes and arcades. Currently they are only use for betting activities and playing tournament poker. However, with the introduction of online casino games, players will be able to play slot machine games online through Totems, the same product that VLTs will be offering, competing directly with licence holders.

Technical And Venue Requirements For VLTs

Technical and venue requirements for VLTs have been regulated by Decree of the 22 of February 2010. An English version of the decree can be found [here](#).

The maximum cost of an individual game in VLTs will be €10, with a minimum stake of €0.5. Players will be able to pay with:

- coins and/ or banknotes;
- technology based on ticket systems;
- prepaid cards;
- registered gaming accounts operated with smart cards;
- reinvestment of previous winnings.

The decree establishes that a minimum of 85 percent of the stakes must be returned to players. The maximum payout on a single game is €5,000 although larger jackpots are allowed. Jackpots can reach €100,000 in the case of one gaming room and €500,000 in the case of a gaming system.

Regulations with regards to the gaming system's technical requirements are contained in article 4 and 5 of the decree.

VLTs can be installed in:

- Bingo halls as per Decree No 29 of 31 January 2000, issued by the Minister of the Economy and Finance, which have an area dedicated to gaming with the machines referred to in Article 110(6) of the T.U.L.P.S., in a proportion not exceeding one third of the area currently used for playing bingo;
- Agencies for betting on sporting events other than horse races and on non- sporting events pursuant to Decree No 111 of 1 March 2006 issued by the Minister of Economy and Finance, the standard agreement for which was approved by Directorial Decree 2006/22503/ Giochi/ UD of 30 June 2006;
- Agencies for totalizer and fixed- odds betting on horse races pursuant to Presidential Decree No 169 of 8 April 1998, the standard agreement for which was approved by Inter- Directorial Decree 2006/16109 of 12 May 2006;
- Gaming shops pursuant to Article 38(2) and (4) of Decree- Law No 223 of 4 July 2006, whose primary activity is marketing public gaming products;
- Public gaming rooms specifically set up for the conduct of lawful gaming, providing a separate area for games reserved for underage players;
- Premises dedicated exclusively to gaming with machines as per Article 110(6) of the T.U.L.P.S.

Venues will be able to have a maximum of 150 VLT machines; however smaller caps will apply to venues that have gaming rooms smaller than 300 square meters.

5. Lotteries**5.1. Statistics**

The overall turnover for lotteries in 2007 was just over €16bn. For 2008, lottery games generated bets for

€17.635bn

For 2009, the results for lottery games were the following:

Lottery game	Gaming Revenue 2009	Variation in relation to 2008	Government collection
Lotto	€5.664bn	-3.2 percent	€1.565bn
Superenalotto	€3.776bn	50.5 percent	€1.235bn
Traditional lottery and other games (scratch, remote, etc)	€9.434bn	1.7 percent	€1.659bn
Total:	€18.874bn		€4.459bn

Source: AAMS

The principal lottery activities operated in Italy are the following:

- Superenalotto.
- Lotto.
- Instant, traditional and remote lotteries.

5.2. Legislative Framework

Lotto

The following are the principal regulation that deals with lotto:

- Law No. 528 of August 2 1982: this law laid out the regulatory code for the running of the game and the personnel who would run it. This law was amended by Law No. 85 of April 19 1990, which gave the State the right to run lotto indefinitely.
- Ministerial Decree of March 17 1993: this decree authorised the giving of the lotto concession to Lottomatica. This decree was further confirmed by Ministerial Decrees of April 17 and June 26 1998.
- Law No. 724 of December 23 1994: this law outlined provisions relating to retail outlets for lotto games.
- Ministerial Decree No. 691 of December 27 1996: this decree dealt with lotto draws.
- Law No. 449 of December 27 1997: this law related to the giving of a sum of the lotto tax revenue for culture and the environment.
- Ministerial Decree of February 9 1999: this decree was a step in remote gaming, for it authorised the taking of lotto bets over the phone. However, this telephone service was suspended in 2005, through the Ministerial Decree of June 7 2005.
- Ministerial Decree No. 474 of December 13 1999: this decree dealt with the sums lotto retail outlets needed to pay the State.
- Ministerial Decree of January 23 2001: this decree raised the maximum lotto bet.
- Law No. 311 of December 30 2004: this law simply paved the way for another weekly lotto draw.
- Decree of June 23 2006: this decree introduced instant lotto, and the ways in which it could be organised and played.
- Decree of May 16 2007: this decree allowed for the issue of new retail outlets with concessions.
- Law No. 296 of December 27 2006 (Article 1, Paragraph 89) (the law which approved the 2007 Budget): this law allowed AAMS to expand the lotto portfolio, allowing for additional and complementary games.

SuperEnalotto

The main legislative decrees which make up the legal framework for SuperEnalotto and SuperStar are:

- Ministerial Decree of July 9 1957: this decree established Enalotto.
- Ministerial Decree of October 29 1957: this decree established the regulation of Enalotto. This decree was amended by Ministerial Decrees of October 10 1997, July 30 1998, September 23 1999, and April 26 2005.
- Law No. 16 of February 27 2002 (was formally Decree No. 452 of December 28 2001): this law abolished the limit on the jackpot, along with permitting the game of SuperEnalotto to be run in other ways.
- Law No. 311 of December 30 2004 (which approved the 2005 Budget): this law allowed another weekly draw of lotto (as mentioned above), including SuperEnalotto.
- Decree of June 29 2007: this decree, as touched upon above, implements parts of the Law No. 296 of December 27 2006 (Article 1, Paragraph 91 of that law) by extending the Sisl's concession to run SuperEnalotto and SuperStar.
- Director Decree No. 2009/21729/ giochi/ Ena issued in June 2009 regarding the regulation of Enalotto
- Director Decree No. 2009/21730/ giochi/ Ena issued in June 11 2009 regarding the regulation of Superstar.

Instant, traditional and remote lotteries

Legislation which concerns traditional, deferred draw lotteries includes:

- Presidential Decree No. 1677 of November 20 1948: this decree regulated the turnover of lotteries and approved the certain national lotteries.
- Law No. 722 of August 4 1955: this law set a maximum of 12 national lotteries and one international lottery (to be run once a year). Other deferred lotteries were added to this list in 2003.

Legislation which concerns instant and instant remote lotteries includes:

- Law No. 62 of March 26 1990: this law authorised the launch of the Gratta e Vinci lottery, which launched in 1994.
- Ministerial Decree No. 183 of February 12 1991: this decree regulates national instant lotteries.
- Law No. 133 of February 26 1994 (implemented Legislative Decree No. 557 of December 30 1993) and Law No. 354 of November 23 2000 (implementing Legislative Decree No. 268 of September 30 2000): these laws defined the means of authorising and granting of licences to manage instant lotteries.
- Law No. 323 of June 20 1996: this law regulated the commission that retailers were allowed to take from ticket sales.
- Law No. 311 of December 30 2004 (the Financial Law 2005): this law regulated the introduction of remote lotteries.
- Decree of September 26 2007: this decree sought to increase the winnings from instant lotteries, and the possibility of reserving tickets in retail outlets.
- Decreto Anti crisi (converted by Legge 3 agosto 2009, 102).

The following are specific managerial decrees which also regulate online/ remote lotteries:

- Managerial Decree of April 13 2006: this decree created remote instant lotteries and the subsequent 18- month trial from the date of introduction.
- Managerial Decree of September 28 2006: this decree set out technical and suchlike aspects of the trial.

5.3 Licensing

Lotto

Lotto is based on 90 numbers, with players needing to guess one to five numbers on the same draw wheel or on all 10 wheels. Recent changes have added another wheel, with a 'fixed draw' allowing players to bet on the position in which their number will appear. A maximum of 10 numbers can be chosen on every card.

Lotto is not played on a pari- mutuel basis, instead the game is played against a bank, with any winnings being in proportion with the odds of the selections.

There is a minimum stake of €1, increasing by units of €0.5, with a maximum bet of €200. The maximum a player can win is €6m.

Another recent addition to lotto was the introduction of 'instant lotto' in 2006.

AAMS took over the running of lotto in 1994 and subsequently handed the management over to Lottomatica S.p.A. (part of the Lottomatica group) via an exclusive concession in 1993. Lottomatica's concession lasts 9 years at a time, having been renewed for the same period each time. The current 9- year concession runs until 16 April 2012.

The concession involves the running of both deferred draw and instant lotteries. In July 2006 Lottomatica introduced Lotto Istantaneo (instant lottery), a game that allows players an option to participate in an instant draw game using the same number of selected for the Lotto game.

As compensation for its management of Lotto, Lottomatica receives a fee equal to a percentage of the amounts wagered. Lottomatica is required to provide a performance bond in an amount equal to 0.3 percent of the total wagers to the AAMS to guarantee performance of Lottomatica's obligation pursuant to the Lotto concession.

Upon termination of the Lotto concession, Lottomatica is required to transfer free of charge to AAMS the ownership of the entire automated systems which relate to the operation of the Lotto game.

SuperEnalotto

A numbers game called Enalotto was originally launched in 1957. With major changes to the rules and formulas of this game under new regulations in 1997, the game name was changed to SuperEnalotto. SuperEnalotto is coupled with the lotto draw.

To play SuperEnalotto players need to guess the first six numbers and the numero jolly - joker, which match up with numbers drawn on the Lotto wheels. What distinguishes this game from lotto is the chance to win very large amounts resulting from a jackpot mechanism, in which prizes not paid out are accumulated into a single large jackpot, paid out only for the hardest and least probable combination - a full six numbers. The first record jackpot awarded in 1998, when the equivalent of €33m was won. A jackpot in 2005 was worth €7m.

The minimum bet is €1, with the player able to make two guesses.

An optional game was introduced in 2006 - SuperStar, which involves picking the first number to be drawn in the national Lotto draw. This game multiplies the winnings from SuperEnalotto (from 20 to 100 times), and also gives the player a chance to win instant prizes.

In 1996 Sisal S.p.A. secured an exclusive concession to run SuperEnalotto. However, following a ruling of the European Court of Justice in November 2006 which heavily criticised AAMS's move to extend in 2005 the exclusive concession to Sisal for another 9- year without soliciting any alternative bids, AAMS was forced to call a fresh licence tender in late 2007. Notably though at the end of the tender process in January 2008 Sisal's bid still resulted as the winning one so the company will continue to hold the exclusive SuperEnalotto licence until 31 December 2015.

Traditional lotteries and instant lotteries (Lotterie Nazionali / National Lotteries)

Traditional lotteries (deferred draw) and instant (scratch/ card, 'Gratta e Vinci'), are currently the two main types of national lottery, with a third type of online lottery in a trial phase.

When AAMS was given the role of running lotteries in 1998, a General Gambling Committee (Comitato Generale per i Giochi) was also established as a supervisory body, charged with the responsibility for the regulation, supervision, control and managing Italy's national lotteries.

Through an exclusive concession of October 14 2003, AAMS granted Consorzio Lottomatica Giochi Sportivi (R.T.I. Lottomatica S.p.A.) the right to run both deferred draw and instant national lotteries. The concession lasts six years, with the concession holder starting to manage deferred draw lotteries in March 2004, and instant lotteries in June 2004.

Deferred draw lotteries are drawn on a fixed date, at the premises of AAMS, under the supervision of the General Gambling Committee. Traditional lotteries are usually run in association with historical, cultural or heritage events. In 2007, four traditional lotteries took place. Prizes ranged from €500,000 to a maximum €5m on the basis of the number of tickets sold.

Instant lotteries are simply played on scratch cards (Gratta e Vinci). There are different prize categories, from €150 (can be collected immediately) up to €5,000 (collected through banking channels) and over €5,000 (which are paid out by licence holders, with the payment type chosen by the winner).

In October 2003, the Ministry of Economy granted to Consorzio Lotterie Nazionali (a consortium with a 63 percent participation of Lottomatica, 20 percent participation of Scientific Games International Inc, 15 percent participation of Arianna 2001 S.p.A. and 2 percent others) the exclusive concession to operate instant and traditional lotteries. The concession expires in March 2010 with respect to traditional lotteries and May 2010 with respect to instant lotteries, unless the terms are extended at the discretion of the AAMS. Instant and traditional lotteries are available at over 47,000 points of sale (of which approximately 34,000 are also Lotto point of sales) but also in bars, motorways, restaurants and newspaper stands.

As compensation for its management of the traditional and instant lotteries, Lottomatica receives a fee equal to a percentage of the amount wagered.

New tender process for instant lotteries

Italy is moving from a single concession for instant lotteries (scratch lotteries- Gratta e Vinci) with Lottomatica and its partners to a multi- concession regime of up to four operators. The tender conditions have recently been made public through the Decreto Anti- crisi converted in law in August 2009 (see point 3.2 and Annex I of this report).

Bids had to be presented by October 12, 2009 and be accompanied by a bank guarantee to the value of €5m. Those who win a licence will have to provide further bank guarantees: €40m to cover the initial period of eight months between the announcement of new licence holders and the beginning of operations, and for the duration of the licence, €75m as guarantee for tax revenues.

The conditions for the operation of the scratchcard business will see 11.9 percent of turnover going to the operator, of which 8 percent is payable to the reseller network, and the licences will run from June 2010 to May 2019.

The complete list of terms and documentation regarding the instant lottery tender process can be found [here](#).

However, in November 2009 the Administrative Court of Lazio cancelled the invitation to the tender procedure as it considered that the tender conditions benefited the current operator Consorzio Lotterie Nazionali led by Lottomatica. The demand that had been filed by Lottomatica's competitor Sisal argued that the tender procedure was against Italian Law and EU regulations, a position that the Lazio court came to agree.

AAMS and Consorzio Lotterie Nazionali have already appealed the Lazio's court decision to the Council of State (Consiglio di Stato) and the case will be decided on March 9th 2010. In the meantime, there is speculation about the future of the Gratta e Vinci game as Consorzio Lotterie Nazionali's lottery concession expires in May 2010.

6. Betting

6.1. Statistics

Betting activities can be divided in the following two categories:

Sporting games (Giochi a base sportive): This category includes games such as sport betting (scommesse sportive a quota fissa) Big, pool betting (concorsi pronostici). In general terms, this area collected bets of €4.085b in 2008, a 44.8 percent increase of the amounts collected in 2007 (€2.820b). According to the AAMS, most of the growth in this sector was generated by sport betting activities as a result of the increase of the number of betting shops and betting 'corners' in Italy. More than 27 percent of the bets were generated through remote channels.

In 2009, sport betting activities collected €4.170bn, 2.1 percent more than 2008, allowing the government to collect €218m in taxes.

Horse racing games: This category includes national equestrian (Ippica Nazionale), horse racing betting (scommesse ippiche) and Totip. In 2008, horse racing games collected €2.272bn in bets, 17.3 percent less than 2007 (€2.748bn). The results of the year 2008 were affected by a strike that closed horse racing activities between October and November of 2008.

In 2009, horse racing activities collected €1.981bn, 12.8 percent less than 2008, revealing the downturn that currently this sector is suffering.

SNAI and SISAL (through its division Matchpoint) are the dominant operators in this market. Other important operators are Lottomatica, Intralot, Cirsa and Coral Eurobet. Most of these operators acceded to their concessions through the 2006 tender organised under the framework established by the "Bersani Law".

Liverpool bookmaker's Stanleybet is an important "unofficial" player of this market. While Stanleybet does not have a government authorisation to operate in Italy, the company actively participates in this market through CTDs (data processing centres) that collect bets from Italian punters in order to be processed abroad. Stanleybet has been litigating for more than a decade in order to support its right to operate in the country, having obtained landmark legal victories before the European Court of Justice in the Placanica and Gambelli cases (see section 6.4).

6.2. Legislative Framework

Horse races

The main modern pieces of legislation, which relate to horse betting are:

- Law of December 23 1996: this law concerned activities connected with the regulation of horse race betting and authorised both the Ministry of Economy and Finance and the Ministry of Agriculture and Forestry the management of these activities.
- Decree of the President No.169 of April 8 1998: this decree deals with the fiscal and management standards for horse race betting.
- Ministerial Decree of June 15 1998: this decree defines the types of bets that can be placed.
- Ministerial Decree of August 2 1999: this decree allowed for new regulations relating to pari- mutuel and fixed- odds betting.
- Ministerial Decree of June 15 2000: this decree introduced regulations regarding telephone betting and betting through an online network.
- Ministerial Decree of November 6 2002: this decree dealt with betting activities passed to TRIS.
- Ministerial Decree of June 3 2004: this decree sought to introduce new regulations for horse race betting.
- Implementation Decree of February 10 2005: this decree dealt with a free-multiple betting procedure relating to totalisator odds.
- Law No. 248 of December 2 2005: this law converted the contents of Decree No. 203 of September 30 2005 into law - dealing with the remote collection of pool betting on horse and sports events.
- Law 248 of August 4 2006: this law established a tender process for the offering of gambling activities
- Implementation Decree of June 6 2007: this decree related to the approval for licences for public outlets and also established a remote network for racing and sports events.
- Decree of June 25 2007: this decree dealt with certain additions and amendments to remote betting (along with bingo and lotteries).

Sports betting, pool betting and other events

The main modern sources of legislation regarding sports and other events betting include:

- Law No. 549 of December 28 1995: this law dealt with the grant of licences.
- Ministerial Decree No. 174 of June 2 1998: this decree dealt with the organisation of pool and fixed odds betting on sports events organised by CONI (the Italian Olympic Committee).
- Ministerial Decree No. 278 of August 2 1999, amended by Ministerial Decree No. 229 of August 5 2004: this decree introduced the possibility of non- sports events being bet upon.
- Law No. 311 of December 30 2004 (the Financial Law 2005): in part this law introduced the framework for remote gambling.
- Law No. 248 of December 2 2005: this law was converted the contents of Decree No. 203 of September 30 2005 into law - dealing with the remote collection of pool betting on horse and sports events.
- Law 248 of August 4 2006: this law established a tender process for the offering of gambling activities.
- Implementation Decree of June 6 2007: this decree related to the approval for licences for public outlets and also established a remote network for racing and sports events.
- Decree of September 17 2007: this decree had regulations concerning remote games and their management.

- Decreto Legge No. 39 of April 28 2009 (Decreto Abruzzo).
- Legge 7 luglio 2009, 88 (Comunitaria 2008).

The relevant pieces of legislation specific to pool betting include:

- Ministerial Decree of July 20 1979: this decree dealt with the management of periodic pools in relation to horse races.
- Ministerial Decree No. 179 of June 1 2003: this decree related to sports betting. This decree was amended by Ministerial Decree No. 228 of August 6 2007.
- The Financial Law of 2007: this law in part, provided for a new type of horse betting competition.

6.3 Licensing

Horse Racing

Legislation regarding betting on horse races in Italy began in 1942, when the State granted the management of betting to the UNIRE (the Italian Equine Association). UNIRE granted the first authorisation to a private company for pari- mutuel betting in 1954 and since the 1990s regulation of sports betting has occurred in connection with UNIRE's interurban pari- mutuel.

Since 1998 the Ministry of Finance has taken on the policy making role in betting activities, while AAMS has been the regulator of this market since 2002.

Betting is organised either via:

- Pari- mutuel betting: the total amount of bets is divided amongst the winners, in reference to the place and last fixed quote (minus the State's share/ tax). The minimum bet is €2.
- Fixed odds betting: through which the winnings are determined by calculating the bet by the fixed odds. The minimum bet is €3.

For horse racing, the most well known form of pari- mutuel betting is TRIS, in which the player needs to guess the first three horses in a race. AAMS with the cooperation of UNIRE, has over the years introduced new forms of horse betting styles: 'Vincente', 'Accoppiata', 'Quarte' and 'Quinte' - each requiring the player to either guess the first, the first two, first four or first five horses in a race.

Since 2006, AAMS has directly managed TRIS, with support from Sisal S.p.A, Consorzio Lottomatica Giochi Sportivi and SNAI S.p.A.

A horse race pool game called TOTIP, was introduced in 1948 by Sisal and remains popular. V7 is a game where multiple bets are placed on horse races. The cost basis of the bet is equal to €0.50 and the minimum bet is €1.

International cooperation in horse race betting has recently seen a project between France and Italy's pari- mutuels unify for some important horse race meets. This began at the end of 2006. During the first half of 2008, a unified pari- mutuel was launched to take bets on some important races in Italy. The bets are taken in real time and managed by AMMS, with support from Sogei.

2008 and 2009 have been a disastrous 18 months for Italian horseracing. The UNIRE governing body was severely criticised by the government for its lacklustre recent performance – leading to a major reorganisation of their structure. Subsequently a scathing European ruling led to a new tender for horseracing betting shop licences which created uncertainty for the 329 "historic" shops that were at the centre of the legal dispute but which continue to make up almost half of total turnover.

Only challenges in the Rome courts by the owners of the shops have prevented their closure, while new shops, operating with licences acquired during this year's tender, will be unlikely to be opening before the last quarter of 2009 and the tender itself was substantially undersubscribed with only 800 of the 3,000 licences on offer taken up.

More fundamentally the horseracing product itself compares unfavourably with sports betting, particularly in terms of returns to punters. While betting on sports is at fixed odds (with only a tiny percentage spent on pools games), racing have been tote only for several decades and only recently have fixed odds been introduced, with many betting shop owners preferring not to offer the product and avoid the risk. This is exacerbated by the perception that many races, especially at minor tracks, are subject to corruption.

Consequently there was little surprise that Raffaele Ferrara, head of gaming authority AAMS, has indicated

that he will be, "fully involved in the relaunch of horseracing in Italy, with even taxation being reviewed."

The Abruzzo Decree introduced some dispositions that look to aid the horse racing industry.

Sport betting and other activities

Sports betting arrived relatively recently in Italy being introduced in 1998. Major changes to sports betting were introduced by AAMS in 2002. These were:

- For fixed- odds betting: the list of events on which bets can be placed was extended to new types of sports and entertainment events, such as: San Remo, movie awards, or current affairs, including the stock exchange.
- For pari- mutuel betting: new game formulas were introduced for: football - 'Big- Match'; motor sports and bike racing - 'Big- Race'.

A football pool, the 'Totocalcio', has been around since 1946, but new styles were recently introduced. 'Totogol' for instance, links the game to the number nine and involves guessing the first nine results on a 'Totocalcio' coupon. - This is perhaps an attempt to stem the decreasing interest in the game, said to be due to the scheduling of football matches on different days and at different times.

Licences to collect bets are granted via a tender process, which need to comply with EU requirements. The last tender was held in October 2006 and licences awarded in December 2006. They will expire on 31, December 2015. A total of about 16,000 terrestrial licences were allocated (betting shops and betting corners) and 33 pure remote gaming licences were also granted for the first time ever in Italy. An AAMS- granted remote gaming licence entitles the operator to offer local residents a wide range of products covering fixed odds/ pool betting (sports, horse races and other events) as well as skill games (including online poker tournaments).

In the case of pool betting, the outlets are all linked to AAMS's pari- mutuel to record the events in real time. The two types of pool betting are:

- State organised pools: Totocalcio and Totogol, managed by AAMS, with licences granted to Sisal, Lottomatica, and SNAL.
- UNIRE organised pools: Totip, a game based on horse racing, managed by Sisal.

6.4 Stanleybet Court Cases

During this last decade Stanleybet obtained a series of important court decisions that has allowed them to continue collecting bets from Italian players through CTD (data transmission centres). However, the company continues litigating in order to obtain legal recognition in Italy and the possibility of acquiring a government licence. In that sense, in 2009 Puglia's administrative court ruled in favour of Stanleybet CTDs, issuing a precautionary injunction defending its CTD network. Another decision issued by the Italian Council of State (consiglio di stato) ruled that CTDs were not illegal per se because they operated without an Italian gaming licence.

In November 2009 the Court of Cassazione (the Italian Supreme Court) referred a new case involving Stanleybet to the European Court of Justice (ECJ). The questions referred by the Court of Cassazione are referred to the legality of tender requirements established by the 2006 Bersani Law for the allocation of sport betting licences. Specifically, the Italian court questions whether the freedoms of establishment and provision of services regulated by articles 49 and 56 of the EC Treaty can be restricted by a domestic tender system issuing a number of concessions, supported by police licences, in a situation where:

- Holders of previously- issued concessions are protected although new entrants were denied access to the market.
- Competition is restricted because new concessions are prevented from locating premises within a certain distance of existing concessions.
- A concession can be forfeited with a consequent demand against financial guarantees and bonds if the concession holder was also engaging in cross border activities similar to those operated under the concession.

This is the third time a case involving Stanleybet is referred to the ECJ (the previous ones were the landmark cases Gambelli and Placanica)².

7. Bingo

7.1. Statistics

Since it was introduced at the end of 2001, bingo betting increased steadily. However, betting in bingo has decreased in the last two years. While in 2007 bingo collected €1.726bn in 2008 this amount decreased 5.2 percent (€1.636bn) in 2008. According to the AAMS 2008 report, the decline in revenues is the result of the gradual reduction of bingo halls. While in 2001 the government granted 300 bingo licences, in 2008 only 200 were active.

In 2009, revenues were down 7.6 percent as bingo games only collected €1.512bn.

7.2. Legislative Framework

The main pieces of legislation which regulates bingo include:

- Law No. 133 of May 13 1999 and Ministerial Decree No. 29 of January 31 2000: these instruments introduced the playing of public bingo, giving the supervisory responsibility to the Ministry of Finance (subsequently transferred to AAMS), which outlined a framework for the granting of licences via tenders.
- Minister's Directive of September 12 2000: this was the directive which envisaged AAMS as the regulator of bingo.
- Implementation Decree of November 16 2000: this decree approved the rules of bingo.
- Ministerial Decree of November 21 2000: this decree gave the authorisation to grant licences for the management of bingo games.
- Implementation Decree of April 1 2004: this decree enabled and regulated the playing of online bingo via an interconnected network.
- Implementation Decree of March 21 2006: this decree introduced the regulation remote bingo.
- Decree of February 28 2007: sought to revise the way bingo is played and introduced further possibilities to play through remote channels.
- Implementation Decree of January 18 2007: this decree raised the possibility of installing amusement machines in bingo clubs.

7.3 Licensing

Bingo, once known as Tombola, developed parallel to Lotto, and can also be traced back many centuries. The game was played mainly in private until 2001, when the first public bingo halls emerged.

Italian legislation places bingo primarily as an entertainment and social activity and, as such, makes a clear distinction between bingo and other games.

The State via AAMS regulates bingo, granting licences to private individuals to manage bingo clubs.

Interestingly, the possibility of installing slot machines in bingo halls has recently been implemented.

Interconnected bingo halls, in which various clubs are interconnected is another new development. In 2004 AAMS introduced a number of rules and variations of the game in this respect:

- National bingo and simultaneous inter- club bingo: all bingo clubs play all the same game at the same time, which generates a national jackpot. Every player has a chance of winning.
- Group bingo: a number of clubs group together, which creates a jackpot amongst them.
- Electronic bingo: involves games with a national online draw, in which players participate through bespoke terminals.

Furthermore, in 2006 some more provisions were introduced which allow players to participate in 'remote bingo', using their own internet connection, interactive TV, or telephone (mobile or fixed line). To participate, each player needs a personal gaming account with the licence holder. The price of cards for remote bingo varies, increasing in €0.10 amounts, up to a maximum of €5. The remote bingo games are managed by a central system, with a list of the scheduled games available. In 2007 AAMS enacted the online bingo rules. However, this game did not become operational immediately as it was required further regulation.

This regulation was passed in 2009 and is the following:

Director Decree No. 2009/8245/ giochi/ BNG of March 30 2009 No. 96

Circular No. 134 of the 31/07/2009 "Bingo remote participation discipline Decree Dirett. 28/02/2007"

8. Remote Gambling

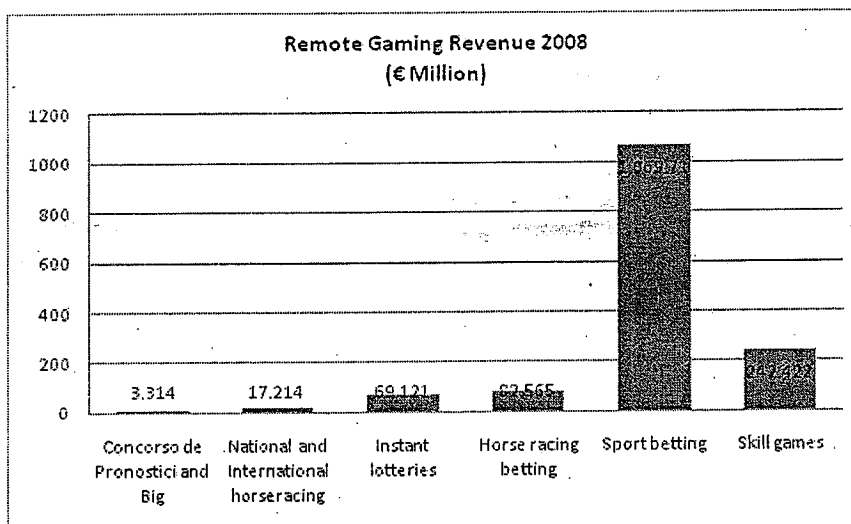
8.1 Statistics

Italy has established in recent years a more open policy towards online gambling. Italy's current position regarding online gambling is that offering certain gambling opportunities is allowed, but only by companies that obtain an Italian licence and only for a limited number of games. While initially, the number of authorised online games was very limited in the last few years it has expanded considerably.

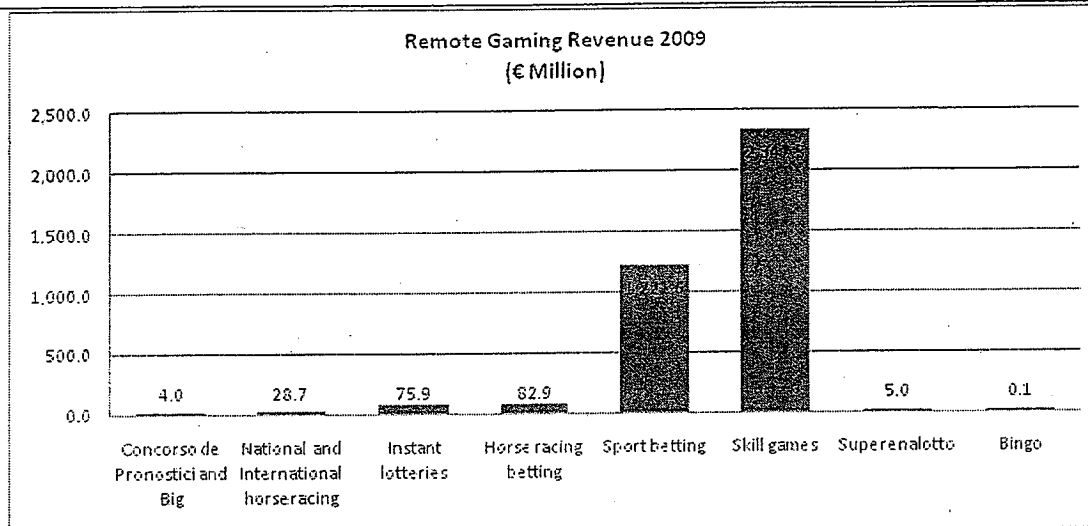
Amongst others, the following games can be offered through a remote platform:

1. International and domestic horse racing betting.
2. Superenalotto, available since July 2009.
3. Instant lotteries ("Gratta e vinci").
4. Sport betting games such as Totocalcio, Totogol, amongst others, available online since March 2008.
5. Skill games, such as tournament poker, available online since September 2008.

In 2008 remote games operators in Italy obtained a turnover of € 1.484bn. The activity that generated more gaming revenues was sport betting, with more than €1bn in bets collected. Surprisingly, the second most profitable operation was skill games (basically, tournament poker) that generated €242m in only four months.



As expected, in 2009 online skill games (tournament poker) become the most profitable online activity in Italy, collecting revenues for €2.347bn, a 868 percent increase from the amounts collected in 2008. 2009 also saw the introduction of online versions of Superenalotto and bingo games in the last months of the year.



Source: AAMS

Games such as remote instant lotteries, Superenalotto and sport betting are managed by the same operators that manage their land- base incarnations. However, that is not the case for poker tournaments games. Gioco Digitale, Microgame and Lottomatica are the operators with the biggest market share in the skill games market. Other companies operating skill games are Pokerstars, Snai, bwin and Sisal.

In 2009 with the enactment of Decreto Abruzzo and Comunitaria 2008, the market has again opened to new forms of online gambling, including cash game poker, bingo and casino games. However, in the case of poker and casino games, further regulation needs to be enacted before they can be operated in Italy.

8.1.1 Online Tournament Poker Games

One of the most significant steps taken towards the liberalization of the market has been the recent opening of the online market to skill- based games such as tournament poker. In the last three years, the Italian Parliament and government have enacted a series of laws and decrees (Decree of March 21, 2006, Decree No. 223 of July 4, 2006, Law No. 248 of August 4 2006 and Ministerial Decree of September 17, 2007), that authorise the provision of skill games through remote media. Operators who want to offer skill- based games to Italian punters need to request a licence from the AAMS and obtain prior approval from AAMS for each skill based game they intend to launch in Italy.

While the regulatory framework for online skill- based games was established in late 2007, the necessity of adapting IT systems to the peculiarities of the protocols required by government operator SOGEI, and integrating their online operations to the AAMS database, delayed the launch of the new skill- based games sites until September 2008.

Some of the most important companies that participate in the remote poker tournament Italian market are:

- Gioco Digitale¹⁰
- Microgame¹¹
- Lottomatica
- SNAI
- Sisal
- Bwin
- Cogotech
- PartyGaming with its brand PartyPoker

The first company that operated tournament online poker was Gioco Digitale. Until April 2009, domestic online operators dominated the market. At that stage, Gioco Digitale had the biggest share of the market, being closely followed by Microgame and Lottomatica. That picture changed in 2010 as international operators have already gained ground and now account for 25 percent of the market¹². In January 2010 Microgame was the leader of the market with a 30 percent participation of the market closely followed by Bwin (which has taken almost 19 percent of the market with the acquisition of Gioco Digitale). Pokerstars now holds the third place as a result of a massive marketing campaign and the signing of local players to its poker team.

Operator	Share of the market January 2010
Microgame	30.2 percent
Pokerstars	17.4 percent
Gioco Digitale	14.4 percent
Lottomatica	11.6 percent
Snai	7.3 percent
Bwin	4.4 percent
LSP	4.1 percent
Eurobet	2.2 percent
PartyPoker	1.6 percent
Cogotech	1.1 percent
Intralot	0.2 percent
Betclick	0.1 percent
Altri	0.3 percent

Source: www.agicoscommesse.it

Tournament poker collected revenues of €2.348bn for 2009, a 868 percent increase from the amounts collected in 2008.

The complete list of operators authorised to operate skill games in Italy can be found [here](#).

8.1.2 Online Bingo

Online bingo went live in December 2009. Bwin's Gioco Digitale was the first operator to offer this game online. According to the data issued by AAMS, while in 2009 online bingo collected €76,194 in bets, in January 2010 this game collected €6.2m.

February 2010 saw the entrance of Microgame into the online bingo sector through its "People's Bingo" brand (www.peoplesbingo.it). Other operators such as Sisal are already offering "play for fun" versions of the game.

However, in February 2009 Lazio's administrative court dealt a major blow to this new industry after establishing that the decrees regulating online bingo (specifically Decree of February 28, 2007 and the Director Decree No. 2009/8245/ giochi/ BNG of March 30, 2009 No. 96) were not compliant with the formalities imposed by Italian Law and ruling that the application of such decrees should be suspended. The court case had been filed by the Assobingo federation, which represents smaller land base bingo operators.

The court decision will interrupt the offering of online bingo in Italy for some time¹³. The Council of State has already filed an appeal to the Court of Appeal in order to overturn the suspension.

8.2 Legislative Framework

Remote gambling for horse racing is principally regulated by Law No. 248 of December 2, 2005 (this law converted the contents of Decree No. 203 of September 30, 2005 into law - dealing with the remote collection of pool betting on horse and sports events); Implementation Decree of June 6, 2007 (this decree is related to the approval for licences for public outlets and also established a remote network for racing and sports events) and Decree of June 25, 2007 (this decree dealt with certain additions and amendments to remote betting, along with bingo and lotteries).

Law No. 311 of December 30, 2004 (the Financial Law 2005) regulated the introduction of remote lotteries.

Remote gambling for sport betting is regulated principally by Law No. 311 of December 30, 2004 (introduced the framework for remote gambling), Law No. 248 of December 2, 2005 (this law was converted the contents of Decree No. 203 of September 30, 2005 into law - dealing with the remote collection of pool betting on horse and sports events), Implementation Decree of June 6, 2007 (this decree related to the approval for licences for public outlets and also established a remote network for racing and sports events) and Decree of September 17, 2007 (this decree had regulations concerning remote games and their management).

In the case of remote tournament poker games, such activities are regulated principally by Decree of March 21, 2006, Decree No. 223 of July 4, 2006, Law No. 248 of August 4, 2006 and Ministerial Decree of September 17, 2007.

The Implementation Decree of March 21, 2006 and Decree of February 28, 2007¹⁴ established the possibility of offering bingo games through remote channels. This form of gaming was regulated recently through the Director Decree No. 2009/8245/ giochi/ BNG of March 30, 2009 No. 96 and Circular No. 134 of the 31/07/2009 "Bingo remote participation discipline Decree Dirett. 28/02/2007". However, the application of this regulation has been suspended by Lazio's administrative court (see section 8.1.2).

Criminal and administrative sanction regime and ISP blocking system

While Italy has been slowly opening its market to online gambling, authorities have established a harsh legal framework in order to deal with illegal operators. First of all, according to article 4 of Law of the 13th of December 1989 No. 401 it is a criminal offence to operate unlicensed gambling by telephone or remote channels. According to article 4 of the law, media companies that advertise the services of illegal operators will also be penalised.

Recently, Comunitaria 2008 introduced some modifications to the Law of the 13th of December 1989, in order to include new sanctions applicable to illegal online operators (see point 3.2 of this report.). This law establishes imprisonment terms from six months to three years to whoever organizes, exercises and collects remotely, without the required licence, any game set up or governed by the AAMS. On the other hand, anyone, even the owner of the licence, who organizes, collects and carries away any game set up or governed by the autonomous state monopolies in ways other than those provided by law shall be punished with imprisonment from three months to one year or with a fine that will range from €500 to €5,000.

Comunitaria 2008 also establishes that a remote licence will be suspended when the operator does not comply with the established technical requirements.

Italian authorities enforce the prohibition against unlicensed operators through an ISP blocking system. Specifically, article 1, paragraph 50 of Law 296 of December 27 2006 (2007 Financial Law) and Directorial Decree AAMS No 1034/ CGV issued on January 2 2007, complemented by Directorial Decree AAMS 1484 issued on June 10 2008, provides AAMS with powers to make it compulsory for internet and other network service providers to block access to remote gambling operators not in possession of Italian licences and included in the list issued by AAMS as indicated in paragraph below.

This regulation authorises AAMS to issue a list of websites providing unauthorised gaming services. The list, which is regularly updated, is communicated to Italian internet service providers (ISPs), which then, under a "notice and take down" obligation, have to deny access to blacklisted websites by redirecting prospective players to an AAMS webpage indicating that they were trying to access a blacklisted website. The latest version of the blacklist, which includes sites managed by Belfair and bwin, names 2,073 blacklisted sites. The most up dated version of the blacklisted sites can be accessed [here](#).

The authority can impose fines on ISPs that range from €30,000 to €180,000 for any breach of their blocking obligations.

The blocking has to some extent barred foreign operators from offering internet casino, lotteries, bets or pools with cash prizes to the Italian public, however several blacklisted websites have been moved to other (and similar IP address) in order to pass through the black- list. These developments have led some European bookmakers to file lawsuits both with Administrative Courts and Civil Courts regarding the blacklisting of their websites. By way and large, the courts have not uphold the appeals, citing reasons of player protection and public order. According to Francesco Portolano, partner at Italian- based law firm Portolano Colella Cavallo, the High Administrative Court "Consiglio di Stato" has recently indicated that the black- list will be considered as valid and enforceable as long as the state monopoly on gaming shall be considered valid under the European and Italian regulations.

8.3 Licensing

Skill games

The Ministerial Decree of September 17 2007, sought to govern the games of skill which are authorised by and regulated by AAMS and offered via the internet, interactive TV and fixed / mobile telephones. The types of games are defined in Article 1 of the Decree as needing to be games in which skill predominates over chance, specifically the "games of skill with cash prizes in which the results depend to a large extent, allowing for the element of chance, on the skill of the players".

According to article 2 of the Decree, in order to obtain a skill games licence, the agent should present an application accompanied with the gaming platform plan. The gaming platform is defined by the Decree in the following way:

"the computerised environment, belonging to the agent's development system, connected thereby to the centralised system and accessible to the player via the internet, interactive television or fixed line or mobile telephone whereby the agent manages and, through the applications of the game, provides the games of skill;"

The game platform plan will also need to be provided when a group of agents join to operate a gaming circuit. According to the Decree, a gaming circuit is defined in the following way:

"The virtual environment, produced between several agents by means of the sharing of the game platform, on which the sessions of the game in which the players who have received the participation rights from the agents themselves are playing take place."

According to article 3 of the Decree, the game platform will need to provide the following:

- Communication in real time with the centralised system and the player;
- The management of the game formulae and the game sessions;
- The sale to the player of the rights of participation and the allocation of the winnings and of the relative payments;
- Providing the player with assistance and information, including the offer of game sessions for learning the game free of charge.

The game platform has to guarantee the correctness, integrity, reliability, security, transparency and confidentiality of the activities and functions performed and the correctness and timeliness of the payment of the winnings. The gaming platform is also responsible for the memorisation and traceability of the gaming sessions data taking place for a minimum period of five years and must adopt solutions which facilitate access of the AAMS to the information for monitoring and inspection actions purposes.

The operator will need to connect its platform to AAMS centralised system. This system is managed by SOGEI, AAMS technological partner.

The price for participation in the tournament may range between multiple sums of €0.50 up to a maximum sum of €100.00.

The value of the winnings, or, in the case in which the same game session allows for multiple winners, at least the value of the highest winnings, shall be greater than the price of the right to participate. The AAMS may through the appropriate provisions define the obligations to be respected in the definition of the sums of the winnings paid out.

The following playing modalities are allowed:

1. Solo playing: where a single player participates.
2. Competition playing: where the game is a tournament style of game of two or more players, playing against each other.

The Decree also allows for both direct and indirect (simply comparing results, where players played independent of each other) contact between the players (Article 6(2)).

In order to obtain a remote licence, operators will need to provide a plan for the implementation of the game of skill. Such plan must cover the following issues:

1. The name of the game;
2. The percentage of the revenue set aside for jackpots;
3. The specific game formula;
4. The value of the participation right charged for each game;
5. The way the game is played, including the time occupied, the ways in which the players interact with the game platform and the rules for determining the results;
6. The rules for determining and allocating the winnings;
7. The rules which regulate the participation of players in competitions, in relation to the level of skill, and those regulating solo playing, defining the levels for judging the winnings;
8. The information made available to the player in respect of the individual gaming sessions;
9. The systems used for managing transmission system and network malfunctions.

The following information and documentation shall be attached to the plan:

1. A copy of the graphics adopted;
2. A complete simulation of the game of skill on ICT support;
3. The information relating to the game of skill and the instructions regarding the methods and mechanisms of the game made available to the player on the agent's website, including the specific safety measures protecting the player of the actual game;
4. The documentation relating to any patents which may have been registered or certifications issued.

In particular, the project must mention the technology that will be used for "geolocation" (systems that identifies the geographical origin of the player that attempts to access the site) in order to prevent Italians have access to non authorised sites managed by the operator.

The latest version of the games of skill protocol – (Games of Skill Protocol Relating to Communication between the Operator's System and The AAMS Validation System Vers. 2.0.) was approved by the Directorial Decree 2008/19582/ Giochi/ SCO del 22 de maggio 2008 2007. The annex that contains such protocols can be access [here](#).

Online bingo

AAMS have already issued the regulation for the implementation of online bingo. The regulation is the following:

Director Decree No. 2009/8245/ giochi/ BNG of March 30 2009 No. 96

Circular No. 134 of the 31/07/2009 "Bingo remote participation discipline Decree Dirett. 28/02/2007"

This regulation contains all the requirements applicable in order to obtain an online licence.

Casino and cash poker games

The Decreto Abruzzo and the Comunitaria 2008 has opened the door for the offering of new remote gaming opportunities in Italy (see point 3.2 of this report). The Decreto Abruzzo opened the door to cash poker. The Comunitaria 2008 established that the following games can be offered remotely:

1. Betting, fixed and totalized, on real or simulated events; including those relating to horse racing and other events;
2. Sports betting and horse racing;
3. National horse racing games;
4. Games of skill;
5. Bets for fixed amount with direct interaction between the players;
6. Bingo;
7. National number games;
8. Instant and deferred lotteries.

The law establishes that the AAMS will need to regulate issues such as definitions, technical requirements, taxes and levies, amongst other issues:

AAMS is entitled to limit to a maximum of 200 new licences to be granted for the games outlined in the previous paragraph. Such licences will have a nine years term.

In the case of remote national number games and lotteries it must be mentioned that Lottomatica holds the monopoly over such activities until 2012. The law therefore provides that the remote licence for such activities can only be granted until the expiration of Lottomatica's licence. Lottomatica will be able to sublicense the remote operation of these games with the prior authorization from AAMS. In that case, Lottomatica will be allowed to charge a premium that cannot exceed the amounts currently charged to physical agents for the operation and distribution of the same games.

According to Communitaria 2008, in order to apply for a remote licence, potential operators will need to comply, amongst others, with the following:

1. They will have to operate of games of chance (even remotely) in one of the states of the European Economic Area (EEA), based on valid and effective licence issued under the provisions of that State, with a total turnover derived from such activity, of not less than €1.5m over the last two financial years before the date of application;
2. Incorporate a legal entity with registered office in one of the states of the EEA before the licence is awarded.
3. The technology infrastructure, both hardware and software, dedicated to the activities must be located within a state of the EEA.
4. In order to obtain a remote licence, operators will need to make a unique down payment of €300,000 plus VAT (20 percent). In the case of online bingo, the operator will need only to pay €50,000 plus VAT.

Companies already operating remote games will pay similar amounts to start operating any of the mentioned new games.

The AAMS has sent to the EU Commission a draft of the regulation for remote fixed odds games and cash poker and the draft was returned without any commentaries, therefore Italy should be in the verge of enacting such regulation. You can review the draft in English in the following [link](#).

The draft will govern remote skill games (organised in tournament and non- tournament style) and remote games of chance with fixed odds and cash prizes, excluding lottery and other related games. The draft regulation is similar in many aspects to the Ministerial Decree of the 17th of September 2007 (that regulates skill games), and it will most likely abrogate this last regulation as it encompasses both the regulation of skill games and fixed odds betting.

One of the most important changes introduced by the draft regulation is that the random number generators of a gaming platform will need to be certified by an accredited testing laboratory.

Section 2.1 of the draft establishes that in order to obtain a remote licence for games of chance of fixed odds the licensee should submit, amongst other documents, "a certificate issued by an accredited

certification body, indicating, among other things, the positive result of the technical inspection performed to determine the conformity of the random number generator."

According to Francesco Rodano at AAMS, the certification will be necessary also for the operators that are already offering online poker tournaments. "We'll create a list of "approved testing houses", that we'll include the companies that meet some requirements. Details on those requirements and on the test that will be required are not available yet" noted Rodano to GamblingCompliance.

The draft also states that any subsequent modifications to any of the platform's essential design characteristics will need to be subject to prior approval from AAMS.

A remote licence will be given to operators who obtain a positive result from the conformity test:

- a) Of the gaming platform design, with respect to the provisions of the decree;
- b) Of the forms of communication of the licensee's processing system with the central system, with respect to the communication protocols established by AAMS.

The requirements of the gaming platform are similar to those established in Ministerial Decree of the 17th of September 2007 (communication in real time with centralised system and player, management of the gaming formulae, etc).

In the case of remote casino gaming and cash poker, the game will need to involve the following:

1. Request by the player of the right to participate in a gaming session authorised by the central system and transfer of the initial bank¹⁵ from the gaming account;
2. Request by the licensee to the central system for validation of the right of participation;
3. Validation and assignment of a unique game code for the right of participation by the central system and the transfer of the unique game code to the licensee;
4. Communication to the player of validation of the right of participation and of the relative unique game code and transfer of the initial bank from the gaming account;
5. Request for participation in an individual hit¹⁶ by the player;
6. Acceptance of the request for participation in a single hit by the licensee and debiting of the relative amount to the bank;
7. Award of any winnings, communication thereof to the player and crediting to the bank;
8. Transfer of the final bank to the gaming account.

In the case of multi-player games, the gaming platform should show players the identity of other players in the form of a pseudonym.

An additional decree has recently been sent by Italy to the EU Commission. This document is currently subject to a standstill period of at least three months that began on December 19, 2009 and which is therefore set to expire as soon as March 19, 2010 (provided that there are no comments from the Commission or other Member States). In brief, this new decree regulates the requirements (tender procedures, guarantees, etc) for online licensees for new and already licensed operators.

An English copy of this draft regulation can be accessed [here](#).

9. Casinos

9.1. Statistics

In the last 35 years, there have only been four licensed casinos in Italy. There are no current official figures of the casino turnover in Italy as these venues are not supervised by a single entity. According to the European Casino Association casinos in Italy collected €564m in bets in 2008, four percent less than the amounts collected in 2007.

Pressure has been mounting in recent years for new casinos to be opened in the country. The most serious proposal is the one proposed by the Tourism Minister Michela Brambilla that will imply the opening of up to 40 casinos in Italy. A first proposal was presented in August 2009 but the parliament dashed the possibility that the draft casino law would be fast tracked.

In February 2010, Minister Brambilla came back with a new draft of the casino bill. The new draft, which was published by Italian weekly business magazine *Espresso*, proposes a maximum of three casinos in each region, located in population centres of at least half a million people and with areas of touristic importance being preferred.

The criteria for the identification of 40 gaming halls to be distributed over all Italy will be established in a special regulation that will be issued under the proposal of the Ministry of Tourism, in coordination with the Ministries of Interior, Justice and Economy and Finance. The new regulation will be issued within 90 days of the new law coming into effect. Regional councils will have an important participation in the selection of the municipalities in which the new facilities will be located.

Brambilla's new proposal would make the four existent casino venues close and they would need to reapply for a licence in order to continue trading.

Gaming taxes for the new venues would be levied on the gross profit margin of the casinos with a sliding scale from 30 percent on margin of up to €25m, to 35 percent on amounts between €25m and €50m, and thereafter a top rate of 50 percent being applied. One fifth of the tax will be destined to fund managed by the Tourism Ministry that will be destined to promote tourism in Italy. The remaining part will be destined to the councils where the casino is located.

The local council will be the major shareholder of the public companies that manage the venues, although the day-to-day management will be subcontracted to operators who will be able to tender for the management of the casinos with licences being issued for a period of nine years. These licences may be renewed once.

AAMS will have the responsibility of overseeing the licence's tender procedure and will need to assure that all the tender requirements comply with EU regulation.

9.2. Legislative Framework

The only four licensed Italian brick- and- mortar casinos (Venice, San Remo, Saint Vincent and Campione) enjoy a special regulatory status which entitles them to offer full- fledged gambling services without contravening the general gambling ban established in the Criminal Code.

Casinos remain one of the few gambling sectors which are not under the supervision of AAMS. Instead casinos are run by local authorities in the provinces and municipalities in which they are located and under the control of the Ministry of Interior. In particular the opening of the casinos has been due, in part to the historical situation of the localities - being heavily linked to international tourism. The relevant localities and authorising decree / law have been:

- San Remo: Royal Decree 2448/1927.
- Campione: Royal Decree 201/1933.
- Venezia: Royal Decree 1404/1936.
- Saint Vincent: Laws 1065/1971 and 690/1981.

As noted above, the Ministry of the Interior controls the authorisation for casinos, specifically the Direzione Generale dell'Amministrazione Civile - Divisione Enti Locali - Sezione 3.

The Constitutional Court (Corte Costituzionale) has criticised the casino sector of the last few decades - arguing that the sector needs harmonisation in laws.

10. Advertising

The only statute expressly regulating advertising of gaming services is contained in article 4 of Law No. 401 of December 13 1989 according to which media companies that advertise the services of operators non- authorised in Italy are punished with a fine and the imprisonment up to three months. As of today in Italy there are no particular rules on advertising of authorized gaming products.

In addition, there is a general prohibition on unlicensed gambling and the opening of gambling houses under article 718-722 of the Criminal Code.

The TULPS Act also criminalises operators who are not in possession of a licence or concession from offering betting. A violation of this Act can result in a number of penalties.

11. Tax

Gambling companies incorporated in Italy or with a permanent establishment in the country will be subject to Italy's Corporate Income Tax. The tax rate for 2009 is 27.5 percent levied over the corporate profits of the company. A Regional Tax is also due at rates from 2.98 percent and 4.82 percent depending from the Region where the Company is settled; the taxable base is approximately equal to the net operating income with certain costs being non- deductible (e.g. labour costs and interest expenses).

In the case of specific gambling taxation, we must comment that this varies according to the activity that is developed by the operator. During to 2009, the Italian government enacted a significant amount of legislation that has changed the tax regime applicable to different gaming activities. In that sense, we will mention some of the current applicable gaming taxes:

11.1 Slot Machines

Until 2008, the applicable tax for Comma 6a/ NewSlot machines was 12.7 percent of the gaming turnover. However, 2009 Financial Law (Decreto Legge 25 giugno 2008, n. 112 converted into law by Legge 6 agosto 2008, n. 133) increased the tax rate to 13.4 percent.

The new VLT machine to be introduced at the end of 2009 will be levied with a 2 percent of tax applicable over the stakes in the period 2009-2011. This tax will be increased to 3 percent in 2012 and 4 percent in 2013

11.2 Fixed Sport Betting

Before the enactment of Decreto Abruzzo, sport betting was levied with two- tier tax on turnover with 3 percent on single bets and 5 percent on multiple bets. However, Decreto Abruzzo has established that the AAMS may change this regime by providing a new taxation of 20 percent of the revenue deducted by the payment of the winnings.

11.3 Bingo

A tax of 20 percent is applied to the total card sales made by bingo halls. The same tax will apply to remote bingo card sales made by the new remote bingo operators. Nevertheless, Decreto Abruzzo has charged the AAMS to change this regime and to provide an 11 percent taxation of the gross revenue.

11.4 Remote Skill Games

According to the Ministerial Decree of September 17, 2007, fees charged for tournament poker and, in general, for skill- based games are liable to a 3 percent tax. On the other hand, Decreto Abruzzo has established that no tournament cash poker games and new online gambling games to be introduced by the AAMS will be subject to with a 20 percent tax only applicable on the revenue deducted by the amounts returned to the player.

11.5 Lotteries

Fifty percent of the sales of the traditional and instant lotteries and the lotto is paid out as prize money. The retailers receive 8 percent of the sales. With the remaining amounts, 29 percent goes to the state treasury, 7 percent goes to Lottomatica (as operator) and 6 percent is paid as gambling tax. The Consorzio Lotterie Nazionali receives 12.4 percent of the sale of the lotteries and the AAMS receives a 2 percent fee.

In the case of Supernalotto, prize payout is 38 percent of the gross revenue, the retailers get 8 percent, 6 percent in the gambling tax and 5 percent is paid to the operator (SISAL).

As far as concern the AAMS enforcement of the aforesaid provisions, a first decree containing the new taxation on Remote Skill Games and Fixed Sporting Betting has been already issued and notified to the

12. Problem Gambling

Part of AAMS's logo reads "Gioco Sicuro", which means safe gambling - and issues surrounding underage gambling, social responsibility and the prevention of problem gambling are priorities for AAMS. Similar to other monopolies around Europe, Italy justifies its monopoly on gambling (and the power to grant concessions) in part on player protection grounds.

AAMS has listed the contributions it makes to social responsibility/ preventative action as:

- Safeguarding minors from gambling.
- Safeguarding players by setting out rules for transparency, for bets and the mechanics of gambling machines.
- Promoting research and study into problem gambling.
- Collaborating with non- profit organisations and others to promote research and treatment of addiction to gambling.
- Controlling networked machines and other systems of gambling.
- Financial contributions.
- Operators of NewSlot machines are bound to report problems to AAMS and keep players informed about the rules and the way the machines work, promotion of responsible gambling and implementing any campaigns of AAMS.
- A stamp for NewSlot machines called "Bollino NewSlot", which is a quality stamp and ensures the constant monitoring is possible. This is a new initiative and operators taking part are trained on responsible gambling subjects and player protection.

Organisations and associations involved in prevention and treatment of problem gambling include:

- Societa Italiana di Intervento Sulle Patologie Compulsive (SIIPAC)
- Associazione degli ex giocatori d'azzardo e familiari (AGITA)
- Associazione per lo studio del gioco d'azzardo e dei comportamenti a rischio (ALEA)
- Associazione Azzardo e nuove dipendenze (AND)

The Municipality of Rome has an initiative along with other municipalities: "Sportello Infozzardo"

13. Money Laundering

Italy's is a member of the FATF, having undergone a Detailed Assessment Report into Anti- Money Laundering and Combating the Financing of Terrorism:

- Full Report
- Annexes with laws in Italian and English in Sections 1, 2, 3, 4, 5, 6, 7, 8, 9 and 10.

Historically Italy has high rates of organised crime, with groups like the Mafia in Sicily and the Camorra in Naples, involved in many types of criminality from the drugs trade through to political and economic criminality. The FATF evaluation report noted that the existing AML legal framework is very complex, suggesting that more consolidation of existing laws and regulations would result in greater clarity and effectiveness.

The current AML law was enacted in 1991: Decree Law 143 of May 3, 1991 "Urgent provisions to limit the use of cash and bearer instruments in transactions and prevent the use of the financial system for purposes of money laundering law" (as amended and ratified by Law 197 of July 5, 1991). The implementation of AML policies comes under the umbrella of the Ministry of Economy and Finance and the financial intelligence unit. AML compliance functions are conducted through the Ufficio Italiano dei Cambi (UIC), market and prudential supervisors and the Guardia di Finanza (GdF).

Money laundering is criminalised by Article 648bis of the Penal Code. The possession and acquisition of proceeds of crime is also criminalised. Money laundering is punishable by imprisonment for between four to 12 years; and also by fines of up to €15,240.

In 2007 Italy enacted Law of November 21 2007 N. 231 in order to implement Directive 2005/60/ EC (on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing) and

Directive 2006/70/ EC. However, such dispositions did not contain any regulation regarding online gambling. This omission has been corrected through Law Decree of the 25 of September 2009 No. 151 that introduced reporting standards for gambling and betting parlours and online gambling operators. The decree puts physical and virtual betting operators within the scope of money laundering regulation.

Under the new rules, online gaming sites and physical operators will need to verify and identify the identity of all customers where the operation amount exceeds €1,000. The regulation also applies to unlicensed CTD (data transmission centres) that transmit bets to overseas bookmakers.

14. Regulator Details

AAMS Headquarters: Piazza Mastai, 11-00153 Roma

Annex I (Decreto Abruzzo, Legge Comunitaria 2008 And Decreto Anti- Crisi)

In this section we mention the most important innovations introduced by the Decreto Abruzzo, Legge Comunitaria and Decreto Anti- crisi in 2009.

Decreto Abruzzo

Decreto Abruzzo implements a series of measures in order to provide relief to the population of the Abruzzo region. The rules regarding the gambling market are contained in article 12 and they seek to raise at least €500m a year, to be used for the reconstruction of the earthquake zone.

Some of the measures put in place by the Decreto Abruzzo are the following:

New instant lottery

The Decree authorizes AAMS to organise a new instant lottery in support of the region of Abruzzo. The AAMS authority will also be free to introduce new lotteries, pools and numbers games which may be sold outside of the traditional network of outlets such as tobacconists, bars and cafés. For the first time supermarkets will be allowed to offer gaming products, and tobacconists will be allowed to open on Sundays and Bank Holidays.

Online gaming

Article 12 (f) of the Decree has modified the regime applicable to online gambling. This article provides that the following games will be authorized in Italy:

- Remote games of chance provided in exchange of a fixed rate.
- Remote poker- types games other than tournament games.

It must be mentioned that prior to the enactment of the Decree only online poker tournaments, being considered as skill- based games by AAMS, were under certain conditions authorised. This legislation plus the regulation included in the Comunitaria 2008, has opened the way for the introduction of cash games for online poker and the offering of other games of chance through the internet such as casino games and bingo.

However, it must be specified that the new rules set forth by the Decree are not *self- executing*: the Decree requires, indeed, an implementation by means of decrees issued by the AAMS.

A draft of the first of such decrees has been notified by AAMS to the European Commission (notification number 2009/469/ I).

In particular, the notified decree provides, on one hand, for a legal framework on remote skill- based games and remote games of chance provided in exchange of a fixed rate and remote poker- types games other than tournament games (on the other). For example, the maximum amount of the bet is equal €250 for the remote skill- based games, and equal to €1000 for remote games of chance provided in exchange of a fixed rate and remote poker games other than tournament games.

Further, the remote games of chance provided in exchange of a fixed rate and remote poker- types games other than tournament games will be levied with a 20 percent tax only applicable on the net winnings (the amounts not returned to the player); for the remote skill- based games, will be levied a 3 percent tax on the total funds raised (not on the net winnings)

Sport betting

A new tax regime is established in relation to some forms of sport betting. In the case of distance sport betting (Scommesse a distanza) in a fixed mode and in where there is direct interaction between individual players a tax will be levied equivalent to 20 percent of the net winnings. A similar tax will apply to fixed mode sport betting (scommesse a quota fissa).

In a move to make the product more attractive, the maximum payout will rise from the present €10,000 to €50,000 while the minimum stake will fall from €3 to €0.50. Furthermore the strict controls on the range of bets offered will be relaxed.

Another important piece of legislation introduced by the Decree consists in the possibility for operators to offer fixed rate bets on sport and non- sport events not included in the AAMS's portfolio. Under the statutes in force as of today (and up the issuance of the implementation legislation by AAMS), Italian licensed operators can offer in Italy exclusively bets on events included on the official AAMS' program. This on one hand reinforces AAMS control on the events and in particular on the results of the event, but on the other hand constitutes a significant restriction to the operators' activities.

Video Lotteries (VLT)

The Decree also authorizes the experimental introduction of video lottery terminals that are characterised by the following:

- They will be controlled remotely.
- They will have a remote digital random generator of winning combinations.
- The payout for player will be equivalent to 85 percent of the wagered amounts.

The AAMS will need to define the following aspects regarding the operation of the VLT:

- Establish a unique tax for the operation of this machine. The tax will not exceed 4 percent of the played amounts. This rate is lower to AWP (13.4), in order to encourage the implementation of these new machines.
- Regulate the venues where VLT will be operated, ensuring that these machines are placed in environments intended solely for public gaming activities. Also, regulating the space requirements for gaming venues and the number of allowed VLT.
- Regulate the requirements to obtain a licence for a VLT, having to pay €15,000 for the installation of each machine. Existing operators will only be able to obtain VLT licences up to 14 percent of the number of AWP that they already operate.
- Establish new requirements in order to grant the licence to operators regulated by article 14, numeral 4 of the Decree of the 26 of October of 1972 No. 640.

The regulation in relation to the implementation of VLTs was enacted recently (Decree of the 6 of August of 2009).

Horse racing

The Decree changes the distribution of winnings in V7 horseracing pools. The game has been made more attractive with 65 percent of the total stakes being paid out in winnings instead of the present 50 percent.

Comunitaria 2008

The Comunitaria law brings in some stricter controls on gaming as well as clarifying the number and cost of new licences that will be available for online gaming and bingo.

The issues related to gambling are all contained in article 24 of the law. Gambling dispositions contained in the Comunitaria look to control the "spread of illegal games and illegal activities related to remote gaming" (online gambling). In that sense, the law regulates new forms of online gambling and in some cases extends the existing provisions to new games. According to the Comunitaria 2008 the following games came be offered remotely:

1. Betting, fixed and totalized, on real or simulated events; including those relating to horse racing and other events;
2. Sport betting and horse racing;
3. National horse racing games;
4. Games of skill;
5. Bets for fixed amount with direct interaction between the players;
6. Bingo;

7. National number games;
8. Instant and deferred lotteries.

The commented law establishes that the AAMS will need to regulate issues such as definitions, technical requirements, taxes and levies, amongst other issues.

Other important issues addressed by the Comunitaria 2008 are the following:

New online games

According to the Comunitaria 2008 AAMS "has the faculty to limit, according to the market's needs, to 200 the number of licences within the first application of the rule" for the games outlined in the previous paragraph. Such licences will have a nine years term.

In the case of remote national number games and lotteries it must be mentioned that Lottomatica holds the monopoly over such activities until 2012. The law therefore provides that the remote licence for such activities can only be granted until the expiration of Lottomatica's licence. Lottomatica will be able to sublicense the remote operation of these games with the prior authorization from AAMS. In that case, Lottomatica will be allowed to charge a premium that cannot exceed the amounts currently charged to physical agents for the operation and distribution of the same games.

In order to apply for a remote licence, potential operators will need to comply, amongst others, with the following:

- They will have to operate of games of chance (even remotely) in one of the states of the European Economic Area (EEA), based on valid and effective licence issued under the provisions of that State, with a total turnover derived from such activity, of not less than €1.5m over the last two financial years before the date of application;
- Incorporate a legal entity with registered office in one of the states of the EEA before the licence is awarded.
- The technology infrastructure, both hardware and software, dedicated to the activities must be located within a state of the EEA.
- In order to obtain a remote licence, operators will need to make a unique down payment of €300,000 plus VAT (20 percent). In the case of online bingo, the operator will need only to pay €50,000 plus VAT.

Companies already operating remote games will pay similar amounts to start operating any of the mentioned new games.

Technical requirements

In order to operate the new online games, operators will need to comply, amongst others, with the following technical requirements:

1. Players will only be able to access the operator's website after the player has registered in the registration system managed by AAMS. AAMS initial idea of requiring players to enter sites via a dedicated portal that would give access to operators' websites was defeated in the Italian *Camera dei Deputati*.
2. Operators will need to prevent consumers living in Italy from playing on sites other than those operated in adherence with the provisions of their concession. That means that Italian operators will need to preclude Italian players from accessing their global website and restrict them to the local site licenced by the AAMS.
3. Operators must establish tools and guidelines for self exclusion or preventing the access of minors to the games, and this ban has to be visible in the virtual game.
4. Promotion of responsible gaming measures and the supervision of consumers according to the standards established in the Italian Consumer Code, approved by the Legislative Decree 6 September 2005, No 206;
5. Transmission to the central system managed by AAMS of information regarding individual games; the levies and payments on individual accounts of the game, their balances, and, using established communication protocols established by the AAMS, the movement, be identified with appropriate encoding, related to activities performed by players through channels that are not controlled by the central system managed by AAMS.
6. Make available in the time and manner specified by the AAMS upon request all documents and information necessary for the performance of surveillance activities and control performed by AAMS.
7. Consent to provide AAMS with access, in the timing and manner specified, to their premises for purposes of monitoring and inspecting their operations and, for the same purpose, committing to maximum assistance and cooperation to AAMS's officials;

8. Establish bank or mail accounts dedicated to the management of players deposits.

The AAMS will take a maximum of 90 days to review each licence request. If there is no express pronouncement from the AAMS in that period time, the request will be considered denied.

New administrative and criminal sanctions

Comunitaria 2008 also establishes a new sanction regime applicable to offenses regarding the operation of online games in Italy. First of all, the law modifies article 4, paragraph 1 of the Law of 13 December 1989, n. 401, in order to establish imprisonment terms of six months to three years to whoever organizes, exercises and collects remotely, without the required licence, any game set up or governed by the AAMS.

In particular, Comunitaria 2008 established that anyone, even the owner of the licence, who organises, collects and carries away any game set up or governed by the AAMS in ways other than those provided by law shall be punished with imprisonment from three months to one year or with a fine that will range from €500 to €5,000.

This provision makes significantly wider the field of application of criminal sanction for the organization, collection and carrying away of the games set up or governed by the AAMS: prior to the enactment of Comunitaria 2008, indeed, criminal sanction was provided only in case of lacking of the required licence.

Paragraphs 24 and 25 establish the cases where a licence will be suspended when the operator does not comply with the established technical and legal requirements, with particular reference to the obligations arising from the subscription of the application for the licence and the execution of the gaming agreement (also by electronic means) between players and the owner of the licence.

Land based tournament poker

The Comunitaria clarifies that land base poker tournament activities can only be organized when the AAMS regulates such activity. Currently, land base tournament poker is illegal.

Decreto Anti- crisi

The Decreto Anti- crisi converted in law in August 2009 contains a range of gaming- related proposals (including the possible introduction of online casino games) in articles 15 bis and 21. This new raft of legislation may oblige AAMS to re- schedule and amend its roll- out of measures to enforce gambling rules introduced by the recent Abruzzo laws. While some deadlines may be pushed back to absorb the impending legislation, rumours suggest that parts of the implementing legislation covering casino games will be introduced by the end of 2009.

One of the most important subjects regulated by the Anti- crisis Decree is the scratch lottery (instant lottery) tender conditions. Italy is moving from a single concession for instant lotteries (scratch cards) with Lottomatica and its partners to a multi- concession regime of up to four operators. The Anti- crisis Decree has established some of the tender conditions applicable to the scratch lottery tender.

The operator of the scratch lottery will receive 11.90 percent compensation of the revenue and the average value of the winnings for each of the licences granted. Eight percent of this compensation will be payable to the outlets that sell the product. The concession will be granted to the economically most advantageous proposal, considering amongst others, the following criteria:

1. Bidders must provide quality standards that ensure complete security to consumers and that tickets are not alterable or copied. They also need to prove they have a good security system for paying players winnings.
2. The winner needs to secure a distribution network of no less 10,000 sale points that must be active by December 31 2010. Non compliance with this requirement could nullify the concession. Many potential bidders have complained that this last requirement benefits the current operator Lottomatica as this company already runs a complete distribution network.

The scratch lottery concession will have a nine year term divided in two periods, the first one of five years and the last of four years. The continuation of the concession for the second term will be allowed only if the AAMS establishes that the operation of the scratch lottery has been managed correctly over the first period.

According to this new regulation the scratch lottery tender has been launched by AAMS on August 13 2009. The concessions offered will be effective on June 1 2010.

Another issue regulated by the Anti- crisis Decree is some of the conditions regarding the licensing of VLTs. According to the law, operators that already hold AWP licence and new operators can apply for a VLT licence. In the case of new operators, the licence can be granted to Italian or EU companies with proven moral, technical and economic qualifications, through a public tender process based on requirement similar to the ones that were established for the licensing of AWP machines. As was established in the Abruzzo Decree, the law signals that existing operators will only be able to apply for a maximum number of licences equivalent to 14 percent of the number of AWP licences they already hold.

End Notes

¹ 'A market develops and grows well if all the pieces fit perfectly together', Game Spectrum (Issue 2, November/ December 2008).

² Corners licences are primarily designed for outlets that offer other services as their primary revenue driver.

³ Source: http://www.agicoscommesse.it/writable/datiarticoli/04_02_10_m10.htm

⁴ Italy still lags behind in credit- card ownership and specifically in usage of credit- cards on the Internet.

⁵ It is still necessary to provide extensive details such as ID card number, fiscal code – similar to National Insurance number – and complete an actual or virtual registration document.

⁶ Source: Casino Magazine, Barnaby Page "Terminal Velocity".

⁷ Source: <http://www.casinoenterprisemanagement.com/newswire/astro-corp-invests-it...>

⁸ The decree defines gaming system as the technological platform supplying games that enables remote control of the game through video lottery terminals in dedicated environments. The gaming system's computerized network guarantees the connection of all the other components of the gaming system, i.e.

central system;

recovery and back- up system;

gaming room system, or gaming room server, if any;

video lottery terminals, the operation of which is permitted only if they are connected to the central system, either directly or through the gaming room system;

⁹ Source: <http://www.fairplayforsportsbetting.eu/latest-news/further-doubt-thrown...>

¹⁰ An Italian company founded by Carlo Gualandri that implemented the first pay- to – play poker site in Italy.

¹¹ An Italian company that is one of the most important providers of remote skill games.

¹² This is without considering Bwin's share as a result of the acquisition of Gioco Digitale.

¹³ At the moment this report was drafted, online bingo was still working as the court decision had not been notified to AAMS.

¹⁴ The Decree was modified by Decree 16/11/09. See text. <http://www.aams.gov.it/site.php?page=20091211130248873&op=download>.

¹⁵ Bank is defined as the amount of credit available to the player to place bets; Initial bank is defined as the amount of credit which the player requests to transfer from his/ her gaming account so that it will become available for placing bets; final bank is defined as the amount of credit available at the end of the gaming session which is transferred to the player's gaming account.

¹⁶ Hit/ s, are defined as an individual cycle of play, independent of preceding and succeeding cycles, which verifies the availability of the bet and is/ are carried out through the individual or repeated stake of amounts of available credit and the assumption of gaming decisions according to the individual game rules, and concludes with a credit made as the player's stake.

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This article is due for review on: 28 May, 2010

EXHIBIT C

France

16 Apr, 2010 / GamblingCompliance Ltd. / Pat Rodrigue

The French National Assembly approved on April 6 the draft bill introducing a licensing regime for online gambling in France. Despite a referral for review to the Constitutional Court filed by the opposition, observers are still expecting the law to be enacted by the end of April 2010. It remains uncertain whether the new system will be in place by the start of the football World Cup in June.

Recent Update

This update contains information on the latest developments concerning the new online gambling law which initiate a controlled opening of the online gaming market in France. The law was voted by the Parliament on April 6, 2010. This information can be found in the Online Gambling section of this report.

This update also contains, in the same section, the latest information concerning recent case law.

For your convenience, all the substantive updates to this report have been highlighted.

1. Executive Summary

La Française des Jeux (FDJ) is the only legal operator of lottery games in France. FDJ is a state-controlled company, with the French government holding 72 percent of its stock. The shares are not publicly traded and the rest of the company is owned by lottery agents and FDJ employees. The government authorizes the lottery games to be operated by the FDJ and sets the contribution which it must return to the state. The FDJ's budget and accounts are also under strict government oversight. Every lottery games regulation must be published in the *Journal Officiel*, the French official gazette.

The Pari- Mutuel Urbain (PMU) is another state-controlled company which provides bets in retail outlets or in racecourses, it also offers betting on horses by mobile phone or on the internet. The PMU was created in 1930 by multiple horseracing associations that had previously been allowed to offer off-track betting. The PMU became an Economic Interest Group (EIG) in 1985, gathering together 51 non profit racing associations.

France also has a vibrant casino market, with 197 casinos, most of which under the control of one of four large groups (Partouche, Barriere, Joa and Tranchant). While the casinos had drop revenues of over €1.4bn since 2007, a profit increase is likely to return now that casinos can offer Texas Hold'em poker in or outside of their premises. All large casino groups in the country have also expressed their interest in obtaining online gambling licences once the licensing process on the controlled opening of the market starts.

The French National Assembly voted on April 6, 2010 a draft bill introducing a licensing regime for online gambling in France. Observers expect the law to be enacted by the end of April 2010. The so called 'controlled opening' ("*ouverture contrôlée*") of the online gambling market concerns 3 different activities: horse betting, sports betting and "shared games which depend on skills", principally targeting online poker. Casino games are excluded from this partial liberalisation. The licences will be issued for renewable five-year periods, with an unlimited number available to all operators who can fill licensing criteria established by ARJEL. The French government is targeting the World Cup in South Africa, beginning on June 11, 2010, for its market opening.

The government has therefore decided to follow the recommendations of a Senate report from December 2007 that included recommendations that current gambling legislation be overhauled and jurisdictions consolidated.

2. The Gaming Market Today

The gaming sector is economically successful, with an ever increasing number of players. In 2008, the Pari Mutuel Urbain, had nearly 9,400 betting shops and increased its annual turnover by 4.8 percent to €9.262bn. According to France's former budget minister legal betting generates around €30-35bn in sales per year and illegal games (on the internet and through unlicensed bookmakers) bring in an additional €8bn- €10bn. Of

the total revenues of the PMU, over €5bn is redistributed to the State and France's horse industry every year from the money wagered on races. PMU is the largest single gaming operator, with its activities comprising over 26 percent of the €37bn total gaming revenues in France in 2008.

The Francaise des Jeux had, in 2008, over 29m players, 40,000 points of sale and a €9.2b turnover. The FDJ's financial results for 2008 showed a 1.1 percent drop over 2007, marking the second consecutive annual decrease in revenues since a record €9.47bn profit in 2006.

Casinos reported €17.1bn turnover compared to €18.5bn in 2007, marking the first drop in revenues in a decade. There are currently 197 casinos in the country, which employ nearly 20,000 people. The smoking ban which came into effect on January 1 2008 contributed to the significant drop in casino revenues for 2007/2008. Casino operators also claim that the increase in internet casino games and the popularity of online poker have had an impact on their revenues.

3. Casino

The French Home Office in 2004/05 created a casino report, which yields interesting data regarding the casino industry in France. Gambling Compliance has compiled the following charts to collate some of the finding from that report.

In 2005, the major players in the industry (by profits and market share) were as follows:

- Partouche was the biggest player in the industry with 50 casinos, an annual profit of €807.43m and a 30.49 percent share of the French casino market.
- Groupe Lucien Barriere is second, with its 31 casinos and €751.67m annual profit representing 28.39 percent of the market.
- Moliflor (now Joa Groupe), which has been taken over by Canadian operator Loto- Quebec and a UK fund, had 20 casinos in 2005 and a profit of €237.65m. Its share of the market was 8.98 percent.
- Groupe Tranchant with its 18 (now 16) casinos, had a market share of 8.37 percent and an annual profit of 221.55m in 2006.

The most profitable single casino in the country was the Enghien casino of Groupe Barriere with profits of €135.3m. A distant second was Partouche's Tour de Salagny casino who had a turnover of €71.2m. The least profitable venues in the country were the Trinite casino (€32,926 profit) and casino Port- la- Nouvel (€47,807 profit).

In the whole country, the profits from slots machines were at €2.476bn for 2005, up 7.3 percent from 2004. However, table games profits were down 4.56 percent at €171m. This represents combined revenues of €2.647bn for 2005. The slot machines in the most popular casinos such as Enghien have returned daily profits of up to €940 while the smaller regional casinos such as Luz- Saint- Sauveur had machines taking as low as €35 per day.

More recent casino statistics indicate gross revenues of €18.5bn in 2007 and €17.1bn in 2008. Net profits have remained around the €3bn mark except for 2008 when it dropped to €2.8bn, in essence returning to the revenue levels contained in the 2005 Home Office report mentioned above.

3.1 Legislative Framework

The Casinos Act (Act of July 12, 1983) is the main regulatory instrument for casinos in France. Article 1 of the Act makes it unlawful to:

- run a house with games of chance which is open to the public or where the admission is subject to an affiliation;
- establish or run any kind of game of chance in a public space;
- advertising an unauthorised house with games of chance.

Each of these offences is punishable by, respectively, three years imprisonment and a €45,000 fine (7 years imprisonment and €100,000 fine if part of an organised criminal network), six month imprisonment and €7,500 fine, and €30,000 fine.

However, this provision is not absolute as, under article 1 of the Act of the 15 June 1907, casinos are authorised to run and offer games of chance to the public. Casinos may only be run in cities or metropolitan

areas with a population of at least 500,000. An exception is granted to smaller cities only if that location is a resort or of particular touristic importance.

Until 2007, casino players had to pay a fee in order to gain entrance to a French casino. This was in fact a stamp duty which could be purchased for a period of one day to one year. The minimum amount for one day access was €10. The same decree that abolished this stamp duty also included new provisions that require all casino players to register (free of charge) before being allowed to play. This measure was implemented in order to restrict access to minors, monitor financial transactions and enforce self-exclusion programs.

A further measure to the above decree is the permission given to French casinos the right to organise poker tournaments. This development to allow in-casino poker tournaments was aided by casino operator, Groupe Partouche, which tested the new type of poker over a period of one and a half years. In the words of Patrick Partouche "The French regulator came to consider that the Texas Hold 'Em game was a casino game, as it is almost everywhere else in the world, and told me "Ok Mr Partouche if you are willing to try it as a test, test it. Then we can make a regulation." So now Texas Hold 'Em poker is fully regularized. The Groupe Partouche operates 47 casinos in France and now we're offering an average 100 tables of cash game poker every single day".

As reported by GamblingCompliance, land based casino groups Barriere, Tranchant and Joagroupe claimed before a Paris court in September 2009 that internet gaming firms proposing online casino games were acting in violation of French law. Casinos believe that by accepting bets from French customers for online casino games, the foreign gaming firms are violating the above mentioned 1983 casino legislation.

On April 14, 2010, the online casinos companies won their case against the French land-based casinos. Barriere, Tranchant and Joagroupe have seen their complaints dismissed against the online operators for not being able to prove "direct harm" ("prejudice direct"). Tranchant told AFP his intention to appeal.

For more information on this case, please refer to the "Online Gambling – Case Law" section of this report.

3.2 Licensing

Casinos fall under the authority of the ministries of Finance and the Interior, which in turn have set up the "Commission Supérieure des Jeux" ("CSJ") in order to grant licences and administer casino regulations. The granting of such licences has to follow a complex procedure involving the creation of a local government advisory panel. This body is composed of congressmen, mayors and public servants, who examine a certain number of applications for the creation, renewal or extension of casinos during their monthly sitting.

Each application is considered according to a number of criteria varying from the population of a town to local competition, local economic interests, as well as public morality. The CSJ will then issue a positive or negative opinion for the application, which will then be transferred to the Interior Ministry which will make the final decision.

Large Texas Hold'Em Poker tournaments have gained in popularity in France over the last few years and the move is seen as a way for the government to help casino operators compete against unlicensed internet sites and illegal gambling rooms. It also offers casino operators a way to find alternative revenue sources, which may prove vital in the current economic downturn. The casinos will also benefit from offering a legal alternative to poker players who had always run the risk of being arrested if they played in an unlicensed venue. The French police had conducted a number of raids on live games and had always made a point of making their presence felt in large tournaments.

The latest decree makes it possible for a casino operator to organise live poker cash games anywhere on the French territory. While it does not go as far as legalising online poker, which was the main objective of the industry's important lobbying effort in 2008, the decree will likely result in significant financial gains for operators such as Partouche and Lucien Barriere. The popularity of poker tournaments is evidenced by events such as the France Poker Tour (FPT), which attracts thousands of participants.

Oddly enough, the latest championship event of the FPT had to be held in San Remo, Italy. As past events had been subject to police raids, arrests and the seizing of poker chips and cards, organisers had felt that moving the tournament outside of the country was the only way to avoid what they saw as police intimidation.

The limit on the number of qualification events for large tournaments, which had previously been set at 100 per year per casino is also lifted by the latest decree, giving casino groups the opportunity to respond to the

large public demand for Texas Hold'Em poker.

The new decree does not require casino operators to obtain a permit for each event; they must simply guarantee that these will be held in a secure environment with the same level of integrity present in a licensed casino. Operators must however notify the police of each event, at least 21 days in advance. They must also forward a list of the personnel that will be representing the company at each event in order for the police to perform a background check.

Under the new rules, qualification or "satellite" tournaments which have to be cancelled perhaps due to weather or for being undersold can be postponed. The 21 days notice does not apply to a postponed game. The prize for qualification tournaments can now comprise solely of an entry to a higher event without having to add a cash prize. Under previous rules, qualification tournaments also had to offer a monetary prize at the end of each event.

4. Slot Machines

4.1 Statistics

There are approximately 22,000 authorized slot machines in French casinos, up from 13,000 in 2001-2002.

Illegal Machines

In respect of illegal machines, the Senate Report of 2001-2002, contained estimates from the French Ministry of Culture (based upon findings by a university research centre) and an industry body, regarding the number of illegal machines in the French market (and Paris region) and revenues generated. The following is a reproduction of these estimates:

Number of illegal machines	Govt. estimates	French Machine manufacturers Federation estimates
Total	6,000 (1999)	30,000
Paris Region	400	5,000
Revenue Per Machine	30-50,000 francs (€4,500-7,600)	5-40,000 francs (€760-6100)

Source: Senate report p. 236.

Gambling machines known as "machine a sous" were extremely popular in bars and dance halls since WWII and have been banned in France since the 1980's.

The ban has been blamed for driving that trade underground (as is revealed in the table above). While the machines had not been legal before the ban, they were the subject of tacit tolerance. Machines could not be seized because operators would rig them to give out only free play through tokens (playing for free was allowed). The machines did not disburse cash. However, the tokens were often exchanged for money or alcoholic drinks by bartenders.

Now that these machines have been banned, the French Senate fears a new breed of gangster is operating the market. The study mentioned above, concludes that even accepting the lowest estimate of 6000 illegal machines, that would have led to more than 2bn Francs in illegal revenues in 2001-2002.

The French Senate denounced the lack of enforcement by the police, which in turn replied that the administrative work required to prosecute this type of crime was too cumbersome and that seized machines

would be quickly replaced anyway given their small cost (20 000 francs at the time) that could be offset in less than 3 weeks by a machine's average profits, estimated at 30,000 francs a month in 2001-2002.

No in- depth studies have been conducted to monitor illegal machines since 2002 but back then, the Senate noted that the numbers were in "severe progression". It could be argued that the vast increase in legal slot machines, from 13,000 in 2002 to 22,000 in 2009, has contributed to counter the increase in the black market by offering a legitimate alternative to players.

4.2 Legislative Framework

Slot machines are only allowed in casinos, according to the law of the 5th of May 1987 (Loi du 5 mai 1987) and are further regulated by the Decree of 14th May 2007. The new decree restricts one time bets to €50 and allows machines to be linked in order to create a progressive jackpot.

A list of authorized machines and their manufacturers is also established and are installed and maintained by companies called Societes de Fournitures et de Maintenance(SFM). The Ministry of the Interior is given the oversight and licensing powers over the SFMs.

Machines Lobby Group

In 2007, in addition to the Senate conference and European pressure, a coalition of bar owners, hoteliers and the "Confédération des Professionnels en Jeux Automatiques" (CPJA) – the trade association representing manufacturers and distributors of pinball machines and table football games; was set up to protest against restrictions that outlaw, what the group refer to as "soft" or "arcade" gaming machines in the France's network of tens of thousands of cafes and bars.

The CPJA in the past has presented its case for a relaxation of the ban to the Senate, most recently in 2006, noting the decline in pinball tables and other machines which characterize French café culture, providing vital additional income for bar owners, especially in rural areas. The CPJA's latest report tells of a machine business in decline - with the number of permitted machines falling from 300,000 in 1981 to 200,000 in 1997 and to 70,000 in 2006.

The CPJA notes that there were 31 distributors in 1991 against just three today, with employment in the sector falling from 16,000 in 1978 to 3,000 today. The industry body explains this decline on competition by new video terminal products from the PMU and Française des Jeux for the decline, as well as, changes in leisure pursuits.

The CDJA suggests that the type of bingo machines widely available throughout Belgium, which offer a very limited prize for small stakes could be introduced as a first step in reviving the industry in France - with the full legalisation of AWP's, not being lobbied for at the moment. The lobbyist coalition back the CPJA's argument, noting that in Europe only France and Portugal have a total ban of any form of gaming machine outside casinos, whilst there are 250,000 machines in Spain, 227,000 in Germany and 215,000 in the UK, and the German treasury earning, the group indicate, 500 million euros per year from these types of gaming machines.

A CDJA spokesperson has said "in France the State refuses to legalise these machines as they believe they would be impossible to control. In the meantime, however, bar- owners are responsible for verifying the income and payments for all of the Monopoly's (FDJ) games. This limitation on commercial freedoms is denying the State and the catering sector a fortune in income that would contribute to sustaining the life of bars, particularly in rural areas, and it would also ensure the survival of those establishments threatened by the introduction of the smoking ban."

5. Online Gambling

As reported by GamblingCompliance, the French National Assembly voted on April 6, 2010 a draft bill introducing a licensing regime for online gambling in France. Observers expect the law to be enacted by the end of April 2010.

Before the enactment of this law, the legislative framework set out a prohibition on online gambling activities with only the FDJ and the PMU allowed to offer online gambling services. Therefore, any competitor running a website proposing lottery or betting services to the French public could face penal sanctions.

Former France budget minister Eric Woerth presented a draft bill aimed at opening the online gambling

market in France in March 2009.

The so called 'controlled opening' ("*ouverture contrôlée*") of the online gambling market concerns 3 different activities: horse betting, sports betting and "shared games which depend on skills", principally targeting online poker. Casino games are excluded from this partial liberalisation.

The law creates an independent licensing and regulatory authority, *l'autorité administrative indépendante de régulation des jeux en ligne*, or ARJEL. The authority will be in charge of issuing three types of remote gambling licences to operators: sports betting (with both fixed-odds and pari-mutuel or pool betting permitted); horserace betting (pari-mutuel only); and poker.

The licences will be issued for renewable five-year periods, with an unlimited number available to all operators who can fill licensing criteria established by ARJEL.

Operators are not required to have all their company headquarters in France but will need to have their servers ("frontal opérateur") in France, keep French bank accounts and install technology to allow all transactions involving French customers to be audited. Operators established in "tax havens" are not eligible for a licence in France. The act did not define "tax haven" but only mentioned that it was "jurisdictions considered by the international community as tax havens".

The main goal of the law is to channel the illegal gambling activities to the legal activities in respecting objectives of general interest which are the protection of players and minors, the fight against fraud and crime, the prevention of conflicts of interest and the fight against unlawful sites.

Article 1 of the law specifically provides that:

"Gambling activities are not an ordinary trade or a regular service, in accordance with the principle of subsidiarity, they are subject to strict supervision in relation to issues of public policy, public security and protection of health and youth"

The French government is targeting the World Cup in South Africa, beginning on June 11, 2010, for its market opening. In February 2010, former budget Minister Eric Woerth insisted the government's target date was "tight but attainable." He predicted the law would be adopted by the end of March and then published in April along with the series of implementing decrees.

"Then in May, licence applications will be investigated and approvals granted in the time envisaged," he added.

Despite a referral for review to the Constitutional filed by the Socialist Party on April 13, 2010, observers are still expecting the law to be enacted for the end of April 2010 which would be the start of the licensing process.

5.1 Legislative Process (summary)

March 2009: Presentation of draft online gambling bill

The long-awaited draft bill aimed at opening the online gambling market was unveiled by previous budget minister Eric Woerth. Concerns over taxation rates and the funding of French horse racing industry had led to major delays in the drafting of the bill.

A confidential version was notified to the European Commission.

September 2009: ECJ Santa Casa decision

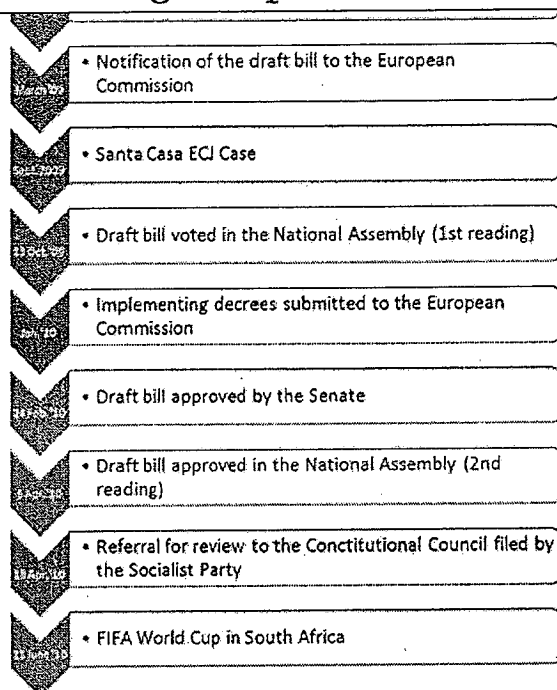
The ECJ for the first time clearly indicated that EU members have strong rights to restrict offers of foreign online gambling services in the name of combating fraud and underage gambling.

October 2009: Draft bill debated in the National Assembly, passed by a 302-206 vote.

The 3 days debates raised numerous concerns. Among other things, legislators voiced their concerns over allowing internet competition that could have a negative impact on the taxation revenues derived by the €9bn-a-year horseracing industry. Amendments were proposed by deputies who are strong supporters of the PMU and FDJ that would ban fixed-odds betting offered by overseas operators. The European Gaming and



• Presentation of the online gambling draft bill by Budget Minister Eric Woerth



Betting Association (EGBA) voiced its opposition of the amendments, which would open the market only to the tote and questioning the requirement for operators to cap their payback ratio. In the first day of discussion in the National Assembly, the amendments to the draft which outlawed online betting resulted in the tabling of last minute amendments which banned betting exchanges such as Belfair.

The bill passed with a comfortable majority of 302 votes against 206.

January 2010: decrees sent to the European Commission

As reported by GamblingCompliance, at the end of January 2010, the French government submitted a series of online gaming decrees to the European Commission as lobbying efforts surrounding France's draft law converge in the key Senate vote the following month. The implementing decrees are still confidential.

February 2010: The Senate approved the draft bill

The Senate voted a draft bill on February 24, 2010.

France's previous budget minister Eric Woerth took this opportunity to insist on the fact that online gaming firms will be obliged to cease accepting bets from existing French customers once the bill is enacted.

March 2010: Debates at the National Assembly (Second Reading)

On the eve of a second reading in the National Assembly of the law regulating the market for online gambling, socialist and communist groups filed nearly 200 amendments in order to challenge the nature of the law or at least delay its implementation.

Some of these amendments were directly contesting the principle of 'controlled opening' of the online gambling market in France. Around fifteen amendments concerned the question of advertising.

April 6, 2010: Final vote at the National Assembly

As reported by GamblingCompliance, votes from the UMP delegation in the French National Assembly allowed President Sarkozy's plans to introduce a licensing regime for online gambling.

The law passed without any change from the version voted by the Senate.

April 13, 2010: Referral for review to the Constitutional Council

As announced by Jean-Marc Ayrault, President of the Socialist Group at the National Assembly, the Socialist Party filed a referral for review of the law to the Constitutional Council on April 13, 2010. The Council can be asked to control the adequacy of the law with the Constitution after the vote of the law by the Parliament and before its enactment by the President. This procedure suspends the enactment of the law. The Council's decision is binding on all authorities and is not subject to appeal.

For more details on each steps of the legislative process, please refer to the relevant articles by GamblingCompliance linked above.

5.2 The Future Agenda

According to the French Constitution, from the moment the law is passed by the Parliament (National Assembly and Senate), the President has 16 days to sign the law. From the day of its signature, the law is enacted. A referral for review to the Constitutional Council can suspend this time and therefore suspend the enactment of the law. As mentioned above, the Socialist Group has filed such referral on April 13, 2010. The Council has 30 days to give its decision but observers expect it to come within two weeks. The law with its possible amendments is to be published along with the Constitutional Council's decision.

The implementation decrees are expected to be published along with the law. They must be reviewed by the Council of State (Conseil d'Etat), France's highest administrative court. Some implementation decrees will also be reviewed by the CNIL (Commission National de l'Informatique et des Libertés), the National Commission for Information Technology and Freedoms. The European Commission will then have to give its agreement.

Sports Federation must also provide the list of events on which they allow betting.

Finally, the Government and the Parliament will appoint members of the College of ARJEL (the licensing board) and the licensing process will start. ARJEL is expecting to look at the applications for licences around mid May.

Jean Francois Vilotte, president of ARJEL declared at a conference in Rome in April 2010:

"The elements of the calendar are working hypotheses. If the text is actually published by mid April, as there has been a temporary authority in place ('mission de prefiguration') and that the book of specifications is already available, ARJEL should be able to review the applications by mid May."

5.3 The New Legislative Framework

Areas covered by the law

According to article 5 of the law, the opening will be limited to "online horse race betting, sport betting and games consisting of shared games which depend on skill". The bill maintains the current pari mutuel system for all French horserace betting, but allows private operators to offer fixed odds betting on other sports competitions. Online poker is allowed, but internet casino games are banned. Therefore, lotteries, virtual slot machines, "spread betting", "betting exchange", betting on virtual competition and casino games in which consumers play against the bank (roulette, blackjack, etc. .) are excluded from the types of online gambling that will be authorised.

ARJEL has specified that an implementing decree, which should be published along with the law, will give an

exhaustive list of the 'shared games which depend on skill' which will be targeted by the law. Poker is certainly covered. Some concerns have risen concerning other type of games: blackjack, bridge etc.

The law defines a gambling game as a "game of chance involving fees, where luck predominates over skills and intelligence for obtaining gain".⁴

Included in the new law	Excluded from the new law
Horserace betting Pari mutuel	Horse betting fixed- odds betting
Fixed- odds betting on other sports competitions	Lotteries
'Shared games which depend on skill' (mainly targeting online poker – a list of the other targeted games will be given later by decrees)	Casino
	Virtual slot machines
	Spread betting
	Betting exchange
	Betting on virtual competition

ARJEL

The law establishes an advisory committee of the games having jurisdiction over all gambling activities. The French newly created gambling regulator is called ARJEL (*"Autorité de Régulation des Jeux en Ligne"* Authority for Regulation of Online Games). It is responsible for collecting the information from supervisory authorities and gaming operators to ensure the consistency of the regulation of gambling industry, issue recommendations on all matters relating to this sector and informing the public about the dangers of gambling.⁵

ARJEL is in charge of issuing the licences for the controlled opening of the online gambling French market. (See details below – Licensing section)

ARJEL gives its opinion on any Governmental project on the online gambling industry. It may also propose to the Government the legislative and regulatory changes that it deems necessary for the pursuit of the objectives of the online gambling policy.

Article 35 of the law provides that ARJEL is composed of a college, a sanctions committee and specialised committees. According to article 43 of the law, the sanctions committee can give the following sanctions:

- A warning;
- The reduction of one year of the 5 years licence;
- The suspension of the licence for 3 months or more;
- The withdrawal of the licence;
- The withdrawal of the licence may be accompanied by a ban from reapplying to a licence for a period of 3 years.

The committee may also impose a financial penalty. The amount must be proportionate to the seriousness of the breach, the extent of the damage caused and the benefits derived from the breach.

Client authentication

Concerning the client identification process, the 'cahier des charges' (book of specifications) imposes on customers to send a proof of identity by post or email to the operator. The operator will then be in charge to send him a letter by post with a code which the customer will use to open his account. The customer will not be able to collect his winnings without showing a proof of identity. Because the operator must send by mail the activation code, it seems that it will be necessary to have human intervention in the identification process.

The entry in the game will be faster thanks to the provisional account, but the exit will be more complicated and longer. It will require the customer to follow all the steps to retrieve his winnings. Each operator must initiate their own client authentication process. The clients' winnings while he has only a provisional account will be blocked for a period of 5 years until he recovers them. It is not explained however what will happen to the money after the expiration of this period if the client does not finalize the identification process.

This particular aspect of client identification raised numerous concerns from operators' side. These formalities have been described as heavy and the operators are afraid that they can be a deterrent to customers. Companies taking in charge the verification of players' proof documents such as Legigame have recently emerged in France.

In order to get around these burdens, operators have mentioned different strategies. Francois Guyot, CEO of Sports Market declared at a conference organised by the GESTE in Paris in March 2010:

"In this market there are many VIP's. 3 percent of players represent 80 percent of the turnover for example. There is much work to be done to the Premium and VIP services to make sure we keep these customers."

Emmanuel de Rohan Chabot from Zeturf declared at the same conference:

"Today things are changing in the context of the law, we will have to find other things to attract customers. Advertising and marketing alright! What about the quality of the product? We must also think about the quality of the service and information. The information requested to customers by the new law is simply incredible. We really have to establish a relation of trust with the client. The least problem encountered by the client, for instance when collecting its winnings, will have great consequences."

Sports Betting Right ("Droit au Pari")

At the heart of the parliamentary debate concerning the online gambling law was the introduction of a "sports betting right" which grant sports teams and federations ownership of information that is currently viewed as being part of the public domain.

Article 52 of the law provides that sports teams and federations have right to adopt regulations for organising the sports events of their fields. This includes the right to consent to the organisation of bets on events or sports competitions. It creates a property right on the final result of the game. However, it does not give any exclusive right to a single betting operator or a trademark right to the sports teams and federations.

Interestingly, the Court of Appeal of Paris confirmed on April 2, 2010 the decision of the Paris Tribunal de Grande Instance from June 17, 2008 which stated that online sports betting companies do not violate in any case the rights of the Paris Saint Germain football club. The Court confirmed in particular that the mere citation of the name of a sports team is perfectly admissible since it is a necessary indication of the online betting activities. In this case, the fact that Bwin's website used the acronym "PSG" to designate the football team to enable the user to gamble was neither an act of counterfeiting nor commercial free riding, the Court stated.

Territoriality

The law gives the possibility for a company which already offers online games in another Member States of the European Economic Area to apply for a licence in France. Operators are not required to have their headquarters in France; they can be located in any other country of the European Economic Area.

However, there are 3 basic elements of attachment to France which are required by the law:

- The 'frontal', or .fr welcoming platform

- The person responsible for the legal monitoring
- The company must appoint a tax representative in France

Operators established in "fiscal paradises" are expressly not eligible for a licence in France.

Revision in 2012

According to article 69 of the law, in a period of 18 months from the date of entry into force of the law, an evaluation report on the conditions and effects of the controlled opening of the online gambling market will be addressed by the Government to Parliament. This report will provide, where appropriate, modifications of the law.⁴

Jacques Myard, Union for a Popular Movement MP in charge of a report on online gambling declared that: "This is the first time that France has a coherent law but it is not perfect, that is why a "clause de revoyure" or "revision option" has been foreseen."

5.4 Licensing

The licences will be issued for renewable five- year periods, with an unlimited number available to all operators who can fill licensing criteria. Three types of remote gambling licences will be issued to operators: sports betting (with both fixed- odds and pari- mutuel or pool betting permitted); horserace betting (pari- mutuel only); and poker. France is expecting 30 to 50 new operators and should give about a 100 licences. Some operators will apply for several licences.

The procedure for the licensing process is contained in the so- called "Cahier de Charges" or book of specifications. This document was drafted as guidelines to be followed by operators in applying for a licence. Just as is the case for the technical standards, the specifications remain in draft form until final approval by the Ministry of the Interior. Contrary to the technical standards, it has not been revised extensively following operator feedback although the ARJEL has published a FAQ section on its website where it answers dozens of queries from prospective licensees regarding the book of specifications.

Licence application packs can be obtained directly from ARJEL. The licence application must be submitted in 5 copies addressed to the ARJEL president and must be in French. All supporting documents in a foreign language must be translated to French. The application must be signed by persons legally authorised to represent the applicant. It must be submitted in person or by registered mail to the ARJEL address in Paris.

In addition to the full identification of the applicant as required by law, the operator must provide information on its finances and accounting, as listed in Sections 3 and 4 of the specifications. Among the most important elements of disclosure are the obligations to reveal: - The identity of any individual owning more than 5 percent of the capital of the company making the application.

- The name of any manager who person with a position of control within the company.
- Any court proceedings against the company or its owners in the last 10 years in France for theft, fraud, blackmail or corruption, money laundering and a number of other offences.
- In the future, if an applicant has not been subject to prosecution but has been subject to an action instituted by ARJEL, for example a foreign operator having been sanctioned under the new law, this must be disclosed to ARJEL.

As for the finances, under article 4 the applicant must demonstrate that it has the capital to support the operation of the gaming activities and that its financial planning is in order. A foreign applicant must appoint a tax representative in France. A financial schedule related to the company's expansion or establishment in France must also be included.

A description of the website and the games proposed must accompany the document (Sections 5 and 6), as well as details on how the applicant intends to operate in relations to player accounts (section 7), outsourcing of operations, internal controls and policies. The applicant must also indicate how it will ensure that no money laundering or other criminal activity takes place on the platform and how conflicts of interest, collusion and cheating will be avoided (Sections 8 and 10)

The document also contains a list of the fees to be paid by licence applicants for each category of online

gaming licence. For sports betting, horse race betting and poker, the fees are listed as €5,000 for a first licence, €8,000 for two licences or €10,000 for three licences. It should be noted that the law only specified that the licence application fee could range from €2,000 to €15,000. As such, experts believed this fee would be higher when it was introduced by ARJEL. Again it is worth mentioning that the book of specifications is in draft form and these fees could still be revised by the Ministry of the Interior.

Although the technical standards deal with the IT requirements imposed on licenses, the specifications (Section 11) mention that on the roll-out of the .fr website, a number of guarantees must be in place, notably as to the terms and conditions imposed on players and data protection measures. The application must also list the measures taken by the operator to prevent problem gambling (Section 9). The applicant can also included any other documents why it considers relevant to the application.

A formal review of this structure will be conducted within six months of the website going live in order to ensure compliance and verify that the guarantees included in the application are indeed in place. The operator therefore has six months to ensure that its .fr platform is fully compliant to the technical standards and the obligations imposed in the law.

The specifications also mention that ARJEL will take up to four months to study the applicant's file and render a decision as to issuance or rejection. It should be mentioned that give the goal of the government to have licensees up and running by the start of the Football World Cup in June 2010, this delay will most likely be shorter than four months and in essence be processed in a matter of weeks.

According to Jean Francois Vilotte, president of ARJEL:

"There will be 3 categories of applications, complete files that can be validated for early June, those whose conditions are not fulfilled which will be rejected and those who require additional documents: the ARJEL will take its time for these ones, considering that it may take up to 4 months to review applications."

5.5 Technical Standards

ARJEL released a draft version of the Technical Standards for online gaming in March 2010. Entitled "Exigences Techniques" or technical requirements, the document and its annex are available in French on ARJEL's website. As of April 15 2010, the document was still in draft form and had been re-published four times with modifications. Although ARJEL has taken a proactive role in modifying the standards following feedback from operators, doubts remain as to whether prospective licensee can integrate those standards into their operation in time for the Football World Cup in June 2010. On this subject, the president of the French online gaming operators association (AFOJEL) and Chilipoker CEO Alexandre Dreyfus issued a statement on April 6, 2010 claiming that it was unrealistic to expect operators to implement an IT structure compliant with the technical standards by June 2010.

One of most important requirements in the structure required by ARJEL is that all French-facing operators adopt a so-called "Frontal Opérateur", which is basically a website with a .fr top-level domain name based on servers located in France. However, the operator is not required to have all of its French-facing operations based on this platform. The .fr platform can be connected to an international operator's other IT structure, what is referred in the document as the "Plateforme Opérateur".

The document gives ARJEL a number of powers regarding the inspection and supervision both at the .fr and international, it also imposes a duty on operators to put in place geolocation mechanisms to ensure that all players with an IP address located in France are directed to the .fr platform. Access to the .fr platform by ARJEL will be also be important, with information such as player's identities, bank details and playing history available to the regulator. The .fr platform will have to be built so that all data passing from it to the operator's servers abroad can be monitored by ARJEL. In that respect, the system differs from that of Italy because ARJEL's role is limited to passive monitoring, with no data passing through its own servers as part of the operations. It should also be note that the level of access for monitoring and the transmission of play data required for poker will be much higher than for betting. This is due to the higher risk of collusion and cheating associated with a platform where players play against each other rather than taking a bet against the operator.

The technical standards specify that this data must be archived securely, a request which has given rise to a debate as to what is considered "secure" retention of data by ARJEL. A point which was raised by operators the release of the technical requirements is that article 4.1.1 of that document states that the operator must retain all 'client-facing' data in such a way that the "integrity, confidentiality and completeness" through mechanisms of time-stamping, linking and tracking.

Operators were worried as to whether Art.4.1.1 requires the data to be verifiable to a standard equivalent to electronic evidence that can be admitted in French Courts. This would thus require operators to observe Art.1316 of the Civil Code, which by decree imposes a minimal technical standard "Z-042-13" to be respected for data to be presented as evidence. One operator was quoted by *igamingfrance* as saying that meeting such a requirement for data keeping would be impossible. ARJEL has moved to dissipate concerns in the FAQ section of its website by stipulating that the requirement is that the data must be stored in a way in which it remains available for one year and must include the player's total wagers, resulting wins and losses and any events. All financial transaction (paying in/out) are also recorded. The players must also have easy access to this data when logging onto his or her account.

The source code of games must also be forwarded to ARJEL for approval prior to a license being issued. The source code of random number generators used in the websites operations is also accessible by ARJEL.

5.6 Payment Process / Site Blocking

Payment under the new regulatory structure is discussed in the law, the book of specification ("Cahier de charges") and the technical standards. The book of specifications contains a requirement in Article 7.4.1 that all licensed operators must have in place mechanisms to ensure that only the player has access to the funds and can withdraw or deposit funds from the account.

The operator must also have in place a system that lets ARJEL monitor all financial transactions by a player. Under Article 7.4.2 of the specifications, this extends to identifying which method of payment (Credit/ Debit Card/ Paypal, Moneybookers, Neteller). ARJEL has indicated in its FAQs to operators that as far as it was concerned there were no extra reporting requirements when players used a payment intermediary and the use of the words "quels que soient les instruments de paiement utilisés" or "whatever payment method is chosen" indicates that ARJEL will not limit how players can fund their account with operators, however the gaming law indicates that further decrees will be adopted which may limit payment methods. Article 7.4.5 does mention that payment intermediaries must have an established presence in the European Union or a country which is part of the European Economic Area having concluded with France a treaty against money laundering, fraud and tax evasion.

The operator must keep the following details regarding players account under 7.4.7 of the specifications:

- The date the account was created.
- A log of all sums paid in and withdrawn by the player within the last year (365 days)
- The player's online gaming wins and losses for a period for the last year.

All payment methods must however be disclosed when applying for the licence (art.13 of the law). Another restriction contained in the law is that players cannot add funds in such a way that it is not traceable ("anonymisant"), which in effect would exclude cash from being used to top up accounts. The law also states that further decrees will list the payment methods that can be accepted and that when a bank account is used, winnings will have to be paid back into the account where the funds have been drawn. This is also mentioned in Article 7.4.3 of the specifications.

The specifications also mention that players must be able to withdraw their winnings at any time and that when a player adds funds, they must be credit to the player account as soon as they clear.

Under article 13 of the law, the operator will have to open an account in the European Union for all of its financial operations related to its platform. When applying for a licence, the operator must also disclose the details of its internal payment processing system.

The book of specifications mentions that new players opening an account must make a declaration that the payment method used is in his or her name (bank account, credit card, e- payment)

A number of reporting duties are also imposed on operators in Article 8 of the specification, notably a requirement to declare suspicious transactions to Tracfin, service of the French Ministry of Finances which fights money laundering and terrorism funding.

At the time that a licensee's website goes live, it must have in place an IT system which tracks financial transactions under the guidelines set out in Section 1.3 of the annex of technical standards. ("Annexe du Dossier des exigences Techniques").

5.7 Advertising

Until their licences have been issued, online operators remain barred from advertising their brand names on the French territory. A number of French football clubs have been negotiating sponsorship agreements with online operators, notably Betclix which has a shirt sponsorship deal in place with Olympique Lyonnais.

One of the main proponents of the gaming reform in France, Senator Francois Trucy, has repeated during the long legislative process which led to the adoption of the new gaming act that the new system would only succeed if the government took action against illegal operators. This would include the enforcement of sanctions against sites which advertise in France without being recognised by ARJEL.

In an interview with clubic.com, Senator Trucy mentioned that without such actions, the situation would return to one where black market operators take the lion's share of the market while legitimate operators are penalised for having gone through the process of obtaining ARJEL approval and agreed to pay licence fees and taxes in France. Trucy added that only one third of online gambling France at the moment was legal and that it would take an aggressive stance against the so-called pirates of the market to change the situation and make the creation of ARJEL and the new licensing process viable.

Trucy added that efforts would also need to be made at the EU level to ensure that there is harmonisation between states implementing gaming reforms in order to block access to the market to unlicensed operators. Trucy mentioned that despite the willingness of ARJEL to fight against illegal websites, any new licensees would have to fight against a largely unregulated competition which is not interested in legitimacy mostly because of issues of taxation and the need to submit to technical requirements. However, he added that in the end, operators who chose to submit to the law would prevail as they will be allowed to operate freely and advertise as they wish while ARJEL pursues their competitors. The opening of the publicity market will also create a war for new players between legal operators and anyone not allowed to publicise their site in France will not be able to participate in this race.

The ARJEL is given wide powers under the law to go after anyone illegally advertising online gambling, with fines of €100,000 to €400,000. Criminal sanctions against online operators can reach three year imprisonment and a fine of €90,000. If the illegal operations are found to have been organised on a larger scale with the participation of more than one company, the fine can reach €300,000 and imprisonment of up to seven years.

5.8 Tax

Article 49 of the law introduces tax rates of 5.7 percent on total stakes for sports betting and horserace betting and 1.8 percent for online poker. These taxes are based on the amounts bet by players. The reinvested winnings as new bets are also subject to these taxes. For poker tournaments in which each player has to pay a right of entry to participate, the tax is based on the total of the collected fees. For other poker tournaments, the tax is based on €0.9 per deal ('par donne').

As reported by GamblingCompliance, shortly after the bill was made public, the tax rates confirmed by budget minister Eric Woerth were higher and raised questions as to how "economically viable" France's online gambling regime would be. Sigrid Ligné, president of the European Gaming and Betting Association (EGBA), expressed some doubts about these previous tax rates. "The 7.5 percent is quite high, and even more so considering the 1 percent extra applied to sports betting to fund the development of sport," said Ligné. "It is very hard to make definitive conclusions as to how viable this system will be."

Even though these tax rates have been lowered, in April 2010, Mangas Gaming vice-chairman Isabelle Parize described the regime as catastrophic and added: "We won't make any money at first. But first-mover is important in this market so we're there".

5.9 EU Perspectives

A New Commissioner: Michel Barnier

In December 2009, Michel Barnier replaced Charlie McCreevy as commissioner for the internal market DG within the European Commission. "The task that I entrusted to Michel Barnier is very clear, is to deepen the internal market in all its dimensions," said José Manuel Barroso, President of the European Commission, when presenting his new team. Michel Barnier's role includes the piloting of policies concerning the free movement of services, goods and capital within the European area.

The new European Internal Market Commissioner gave a broadly neutral speech to the European Parliament saying he would seek coherent EU rules on gambling. As reported by GamblingCompliance, both state and private interests moved quickly to claim his plans supported their cause.

Guido Berardis, director of the Services department of European Commission's DG MARKT declared at a conference in Rome on April 9, 2010:

"The real novelty is the advent of Mr Barnier. He opened a new era and showed a deep interest in the gaming industry. Facing the European Parliament he was clear and convincing and underlined the need for investigation first. He added that 'The goal is not to liberalise [the market] but to bring security to citizens'."

Green Paper

During his introductory speech to the European Parliament, Michel Barnier announced that the Commission would drive forward a debate on cross-border gambling through a Green Paper. A Green Paper typically serves to coordinate an open consultation and to gather information on a specific issue among member states. It can come as an initial step before a Commission White Paper which may then serve as guidance for a possible directive that sets formal EU standards.

Guido Berardis announced that the Green Paper would be ready for fall 2010 – "its findings will appreciate the limitations and needs."

The precise terms of the Commission's Green Paper are thought yet to be established, and it is equally unclear at this stage whether there will be enough common ground as a result of the paper for the Commission to suggest any further action beyond its discussion document.

5.10 Case Law

European Commission

France's strict prohibition on gambling has been challenged by the European Commission. The Commission considered that the French legal regime was infringing the principle of freedom to provide services (contained in Article 49 of the EU Treaty) and decided to open an infringement procedure in October 2006.

In June 2007, the European Commission officially demanded France to initiate changes to its legislation by sending a "reasoned opinion". This constitutes the second step of an infringement procedure under article 226 of the European Community Treaty.

Negotiations between the French government and the European Commission took place in order to modify the French legal framework related to online gambling and render it compliant with European Union law. While the European commission still has to give its approval to the new French law and its implementing decrees, which will most certainly happen, it should logically sign the end of the infringement procedure.

Santa Casa decision – European Court of Justice

French legislators looking for guidance in the adoption of the draft bill may have looked at the decision of the European Court of Justice in the Santa Casa case from September 2009. The ECJ for the first time, clearly indicated that EU members have strong rights to restrict offers of foreign online gambling services in the name of combating fraud and underage gambling. While the ECJ did find that a 2003 Portuguese law giving a monopoly to a government-run charitable organisation over all aspects of online gambling was contrary to principle of freedom of services in the EU, it added that this violation was justified by over-riding reasons relating to the protection of public interest.

In a statement issued after publication of the judgment, French budget minister Eric Woerth said he welcomed the ECJ's decision. Woerth said the decision would "strengthen the architecture of the French legal project" that will require all internet gaming companies to obtain a national licence in order to operate in France from 2010. The parameters set by the judgment in allowing a country to restrict freedom of services within the single market as applied to online gambling were examined carefully by French legislators.

Observers have highlighted that during the 3 days of legislative debates in the National Assembly early October 2009 concerning the online gambling proposals, the decision by the ECJ weighed heavily on the debate, giving strength to the voices opposed to the opening up of the French market to foreign competition.

At a conference in Rome on April 9, 2010, Jean Francois Vilotte, the President of the new French gaming authority ARJEL declared that:

"Italy and France are convinced that there is a need for a regulation of the industry at national level. It is for Member States to regulate this industry because it is not an ordinary economic activity. Italy and France have been delighted to see that this conception has been welcomed by the Santa Casa case"

Asked by Gambling Compliance about his views on the impact of the decision on the French gaming market, Paris-based gaming lawyer Thibault Verbiest, of the ULYS law firm, indicated that the ruling should not be given too broad interpretation and remains, above all, a ruling on the particular legal regime applicable in Portugal with regard to online gaming operators.

Verbiest added that the case needs to be distinguished from the legal regimes applicable in other Member States of the EU and that it stands on its own facts. Therefore, Verbiest believes that online gaming operators can still rely successfully on the freedom to provide services, as enshrined in Article 49 of the EC Treaty in order to challenge national monopolies on online gaming. As is, the ruling does not modify the current state of EC law with regard to the "conditional recognition principle", Verbiest added, mentioning that it is settled case law of the ECJ that a host Member State needs to take account of the conditions fulfilled in a home Member State when the former assesses whether to grant a license to exercise a regulated activity in its jurisdiction.

Verbiest admitted in September 2009 that it was highly likely that the Draft French Gaming Law would be influenced by the ECJ's ruling in Bwin Liga. It was expected that it would be relied upon as an argument by those who are advocating a significant state regulation of, and intervention in, the online gaming sector. Moreover, according to Verbiest, the French Gaming Law is fairly balanced between the requirements of the EC Commission and the margin of appreciation afforded to Member States, as recalled by the ECJ.

Another crucial point according to Verbiest is the fact that the decision had likely strengthened the French Government's position vis-à-vis the EC Commission with respect to its detailed opinion on the Draft French Gaming Law. The EC Commission had criticized, among other things, the proposed licensing system for online gaming operators because it was unclear as to what extent the new regulator ARJEL would have to take into account in assessing whether to grant a licence, the conditions already fulfilled in the Home Member State.

Finally, Verbiest stated that the ruling seems to be at odds with the ECJ's previous case law on the four freedoms (movement of goods, capital, services and persons) and that there are no compelling reasons why the online gaming sector should not be treated equally as other sectors doing business within the internal EU market.

Zeturf Case I (Cour de Cassation)

The facts surrounding the Zeturf case started in 2005, when the PMU (having the exclusive right since 1891 to offer betting on horseracing and gives €650m in support to the industry), issued a summons to Zeturf and a French company, Eturf (formerly directed by the director of the company Zeturf). Eturf was providing Zeturf with data on the races selected for the on-line betting. The summons sought to order these two companies to cease exercising or participating in such an activity with regard to horse races organised in France.

On July 8, 2005, the Paris Court of First Instance ruled that it was illegal for Zeturf to accept bets from French citizens over the internet. The court found that the activity undertaken by Zeturf caused a manifestly illegal nuisance, in that it infringed the exclusive right reserved by law to the PMU to organise, outside of the race tracks, betting on horse races taking place in France. The court ordered:

- Zeturf to terminate such activity on its site (subject to the provisional penalty of €15,000 per day of delay upon the expiry of the 48-hour period following notification of the ruling), and
- Eturf, to implement all resources available to it to cease any contribution to the operation of this activity.

Zeturf appealed, but lost again in the French Court of Appeal, on January 6, 2006. Zeturf also appealed this decision.

However, since the company had relocated to Malta (being sold to Maltese investors, securing a betting licence from Malta), the PMU was forced to pursue Zeturf through the Maltese courts, to enforce the orders. The court in Malta, on administrative law grounds, found that the enforcement of the French orders was inapplicable in Malta.

Shortly after the Maltese court decision not to enforce the judgment, Zeturf's appeal in France's equivalent of a Supreme Court, was delivered (Zeturf, *Cour de Cassation, Chambre Commerciale*, 13 July 2007, RLDI2007/29, n°965). The Supreme Court, in watershed ruling, took the evolution of ECJ case-law into account when determining whether the French legislation regarding the monopoly granted to the PMU was valid under the European Union law.

Abrogating the decision of the Court of Appeal, the Supreme Court found against the PMU, indicating that the monopoly PMU enjoyed was not consistent with EU competition law. In short, the Supreme Court has ordered the French Court of Appeal to take into account guidelines set by the ECJ, when it reconsiders the case, something which the Appeal Court failed to do.

Specifically, the Supreme Court observed that:

1. The mere fact that the State was collecting the gambling gains was not enough to condemn the PMU's monopoly, as well as, any kind of similar restrictive legislation - as long as the objective behind such restrictions was to reduce gambling opportunities;
2. However, the appeal decision admitted the PMU's monopoly was reserved on the basis that it was required to verify whether such a situation corresponded to a consistent social policy of gambling restriction, that is to say, protection of gamblers and fraud prevention. If the state or the betting institutions are pursuing an expansion policy of gambling, then such restrictions cannot be justified.
3. Lastly, the Court applied the European Community principle of "mutual recognition": courts must now verify whether or not the member state, in which the gambling services are located, has restrictive legislation concerning gambling. If such is the case, the restrictions set out by the gambling service recipient's State cannot be justified.

As noted above, the case now refers back to the Court of Appeal, which will be forced to preside over the legitimacy of the French monopoly on betting services enjoyed by the PMU, in light of guidelines set by the ECJ in cases such as Gambelli and Placanica, before imposing any punitive sanctions upon Zeturf.

This decision is a watershed in challenging French legislation on gambling and betting. It has been suggested that this decision was a catalyst for the French Senate conference of last year.

Moreover, with courts needing to consider EU competition law and whether a monopoly is expanding its gambling policy, it may be particularly hard for courts not to consider the advertising campaigns of both the FDJ and the PMU as inciting gambling.

This case is therefore one of the driving forces behind the belief that the current monopolies will disappear in the near future.

In addition, French authorities have placed a moratorium on criminal proceedings against licensed EU operators.

Zeturf case II (Conseil d'Etat & European Court of Justice)

Article 27 of Decree No. 97-456 of 5 May 1997 on the racecourse and horse betting provides that the management of organisation of pari mutual outside of hippodromes has been entrusted to the PMU.

In the framework of a procedure launched by Zeturf Ltd to repeal this article on the racecourse and horse betting, the Conseil d'Etat (France's highest administrative Court) lodged a reference for a preliminary ruling on May 12, 2008 to the ECJ. Pari Mutuel Urbain (PMU) joined the legal debate as an intervening party.

The following questions were referred to the European Court of Justice:

"Are Articles 49 and 50 of the Treaty establishing the European Community to be interpreted as precluding national legislation which has established a system whereby off-course horserace betting is managed exclusively by a single, non-profit-making operator where, although that system appears to fit the purpose of combating criminality and thus of protecting public order more effectively than would less restrictive measures, it is accompanied by a dynamic commercial policy on the part of the operator, in order to neutralise the risk of unauthorised gambling networks emerging and to channel bettors towards the lawful offer, that

does not, in consequence, fully achieve the objective of reducing gambling opportunities?

Is it appropriate, in order to determine whether national legislation such as that in force in France, which has established a system whereby off-course horserace betting is managed exclusively by a single, non-profit-making operator, is contrary to Articles 49 and 50 of the Treaty establishing the European Community, to assess the impairment of freedom to provide services solely from the point of view of the restrictions placed on offering on-line horserace betting, or is it appropriate to take into consideration the entire horserace betting sector in whatever form it is offered and is accessible to bettors?"

According to information collected by GamblingCompliance, all the parties have handed their comments to the Court and Zeturf asked for an oral procedure, which can be refused by the Court although it is rare. The parties are therefore now waiting to know whether they should prepare for a hearing or not.

This case is one of 16 involving 6 EU countries (Germany, the Netherlands, Portugal, Austria, Sweden and Italy) currently pending at the European Court of Justice and touching various questions such as mutual recognition of licences, advertising of gambling in the EU, consistency of national policies of games or equal treatment of potential candidates.

Online casino case

As reported by GamblingCompliance, land based casino groups Barrière, Tranchant and Joagroupe claimed before a Paris court in September 2009 that internet gaming firms, including Vienna-based Bwin were acting in violation of French law. Casinos believes that by accepting bets from French customers for online casino games, the foreign gaming firms are violating France's 1983 casino legislation, which restricts the offering of casino gambling in France to nationally-licensed companies.

"They are violating every single article of this law," said Thibault de Montbrial, Casinos de France's lawyer in the case, who explained that French law allows civil parties to open criminal proceedings where they suffer legal grievance. "We want a French court to acknowledge that all these websites are already operating in the market and that what they are doing is illegal," he added.

On April 14, 2010, the online casinos companies won their case against the French land-based casinos. Barrière, Tranchant and Joagroupe have seen their complaints dismissed against Bwin, Unibet, Sportingbet and 888 for not being able to prove "direct harm" ("préjudice direct"). Georges Tranchant, one of the complainants, creator of the eponymous group of 16 casinos, told AFP his intention to appeal.

The ruling comes less than two months before the opening to the competition of the French online gambling market, which excludes online casinos.

Despite the limited opening, the likes of Barrière and Joa have already confirmed their intention to seek out licences under the new regime to offer poker in France. But the companies are still very much hoping to legally offer online casino games in the future, said John Strock, chief operating officer of Barrière Interactive.

"I think people here now understand that there is a necessary first step for the government to first feel comfortable with poker, and that there could be casino games in around two years time," he said.

"As long as there are casino games at some point in three- to four years time I don't think they'd be too unhappy," Strock added.

6. Lottery

6.1 Legislative Framework

The Act of 21 May 1836 on the prohibition of lotteries ("the Act") sets out a strict ban on lottery activities. The Act is still in place but a number of exceptions have been allowed over the last two centuries.

For the purpose of the Act, lottery was defined as the following (Article 2):

- Any offer made to the public, independently of the name used;
- which promises to fill the hope of a gain;
- acquired through a random outcome.

The violation of this prohibition is still punishable by two years of imprisonment and a €60,000 fine (Article 3). Moreover, the mere advertisement of such activities is punishable by a €30,000 fine (Article 4, al. 2).

Along with the prohibition, the Act also laid out an exception regarding local lotteries for which the profits are exclusively allocated to social or charitable activities.

An important exception to the gaming ban contained in the 1836 Gaming Act is contained in Decree n°78-1067 of November 9, 1978 which authorises a national lottery, organised and exploited by a public undertaking (the French state holds 72% share in the company), La Française des Jeux ("FDJ").

In addition to the legal monopoly for organising Lotteries, the FDJ is also the only company entitled to organise sport betting, through Article 42, Law n°84-1208 of the December 29, 1984.

Due to the monopolistic position of the FDJ, numerous control procedures are set out by the law. The most important one is applied by the Budget Ministry, which determine the stakes as well as the total amount affected to the organisation and the exploitation of the games.

The FDJ is, by law, the only body authorised to propose and organise lotteries and sport betting. This legal monopoly was recently extended to the internet. In practice, this means that any website accessible from France and proposing lotteries and betting services could face penal proceedings.

7. Racing

7.1 Statistics

The PMU accounts for 8,000 sales point, with 14,000 betting machines installed. In addition, bets can be placed using telephone, minitel, as well as, on a thematic TV channel.

Like the FDJ, the PMU's monopoly was extended to the internet. It is therefore the only operator legally authorised to propose such activity.

7.2 Legislative Framework

The monopoly granted to the FDJ does not extend to horse betting. Indeed, the Act of June 2, 1891 reserves a monopoly for this specific type of betting to the (PMU).

This legal monopoly, in practice, is translated into an organisation with impressive economic performances, having seen its turnover rise to €8.84b, an increase of 9 percent.

8. Tax

The State deduction on the gambling activities of casinos is on the gross proceeds of the games. It is defined as the daily gross turnover ('DGT') on each gambling tables or slots.

The first deduction takes the form of a lump sum payment which cannot be the subject of any allowance. The DGT varies depending on the type of gamble :

- for 'traditional' gambling : 0.5 percent paid to the State
- for slots machines : 2 percent paid to the town where the casino operates

Once the first deduction is paid, two allowances are carried out before a second graduated deduction is calculated.

- the first allowance is automatic and accounts for 25 percent chargeable basis;
- the second allowance is facultative and cumulative with the first allowance only if the casino host artistic event. It accounts for 10 percent.

The graduated deduction on the DGT is then calculated. It was created by the 19 December 1926 Act and its scale is, since the 1st November 1988, as follows:

Scale (percent)	Bracket
10	until 290,000
15	from 290,000 to 575,000
25	from 575,000 to 1,775,000
35	from 1,775,000 to 3,300,000
45	from 3,300,000 to 5,500,000
55	from 5,500,000 to 16,500,000
60	from 16,500,000 to 27,500,000
65	from 27,500,000 to 38,500,000
70	from 38,500,000 to 49,500,000
80	above 49,500,000

9. Problem Gambling

While many books and articles have been published in France over the last decade on the subject of problem gambling, the last analysis resembling a prevalence study dates from 1993. Using a questionnaire similar to the DSM- III, the authors found that the prevalence rate in France was around 2%. The study was conducted by interviewing subjects aged 25-44 who were users of the Gambling helpline *SOS Joueurs*. Because the study was done by interacting only with people who sought the use of professional help for their gambling addiction, it does not reflect the status of gambling within the general population. The prevalence rate was estimated by comparing sample rates to other jurisdictions with similar surveys. The study did find that amongst callers to SOS Joueurs:

- 19.3 percent admitted to have committed criminal acts in order to fund their gambling addiction
- 96.6 percent said they had past or present gambling debt.
- 15.7 percent had divorces/ separations related to their gambling problems.

The serious lack of current statistics and funding is denounced by one of the authors of the 1993 study in this document. A new study entitled *l'Expertise collective de l'Inserm sur le jeu pathologique* was published in July 2008. The Inserm (Institut National de la Sante de la Recherche Medicale) is French public organization dedicated to biological, medical and public health research. The study was more of a market overview,

examining player participation and gaming enterprises revenues. The study noted that since 1978, the amount of money wagered annually by French citizens has grown from €98m to €37bn. The study also found that over 30m people had participated in some form of gambling in the French territory in 2006. The study mentions that problem gambling rate in the country stands between 1 and 2 percent of the adult population, or percentage that translates to 400,000-800,000 people.

A French non-profit organization called Adictel has developed a support system for online players and their contact details are present on many French language online casinos. Adictel has also introduced a seal or approval for online gaming site it considers ethical. Adictel's popularity on French sites and its pioneering online support methods has led many operators from other countries to adopt its services. The site is now translated in 7 languages and offers 24 hour live help. Discussion forums moderated by qualified psychologists have also been introduced.

Problem gambling or "Jeu Pathologique" is one of the areas dealt with by the French health ministry's plan to combat addictions or "Plan de prise en charge et de prévention des addictions (2007-2011)" which seeks not only to reduce the prevalence rate but also examines the effectiveness of resources to combat problem gambling.

10. Money Laundering

Money laundering initially became a concern in France shortly after the creation of the Financial Action Task Force in 1989. It is subject to a number of laws and decrees.

By decrees of the 9 May 1990, two public organisations, TRACFIN and the OCRGDE, have been created. Both these organisations monitor and prevent money laundering.

By law, money laundering is deemed a general criminal offence under the Act of May 13, 1996 which inserted the following sections into the Penal Code:

"Article 324-1 (Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996) (Ordinance no. 2000-916 of 19 September 2000 Article 3 Official Journal of 22 September 2000 in force 1 January 2002)

Money laundering is facilitating by any means the false justification of the origin of the property or income of the perpetrator of a felony or misdemeanour which has brought him a direct or indirect benefit.

Money laundering also comprises assistance in investing, concealing or converting the direct or indirect products of a felony or misdemeanour.

Money laundering is punishable by five years' imprisonment and a fine of up to €375,000.

Article 324-2 (Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996) (Ordinance no. 2000-916 of 19 September 2000 Article 3 Official Journal of 22 September 2000 in force 1 January 2002)

Money laundering is punishable by ten years' imprisonment and a fine of up to €750,000:

1. where it was committed habitually or by using the facilities offered by the exercise of a professional activity;
2. where it was committed by an organised gang.

Article 324-3 (Inserted by Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996)

The fines referred to under articles 324-1 and 324-2 may be raised to amount to half the value of the property or funds in respect of which the money laundering operations were carried out.

Article 324-4 (Inserted by Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996)

Where the felony or misdemeanour which produced the property or funds for which the money-laundering operations were carried out is punishable by a custodial sentence higher than that incurred under articles 324-1 or 324-2, the offence of money-laundering is punishable by the penalties applicable to the offence the money-launderer knew about, and if this offence was accompanied by aggravating circumstances, by such penalties as relate exclusively to the circumstances of which he was aware.

Article 324-5 (Inserted by Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996)

As regards recidivism, money laundering is assimilated to the offence for which the money laundering operations were performed.

Article 324-6 (Inserted by Act no. 96-392 of 13th May 1996 Article 1 Official Journal of 14th May 1996)

Attempt to commit the misdemeanours referred to under the present Section is subject to the same penalties."

The provisions apply to the gaming sector, especially to casinos, which are heavily monitored by the aforementioned organisations. By an act of the 15 May 2001, casinos are required to submit to TRACFIN the identification of clients, report any unusual or suspicious financial transactions and set out an internal control system.

By law, the FDJ and the PMU are also required to submit to TRACFIN the identification of clients.

11. Legislation

The Casinos Act (Act of July 12, 1983)

Decree of 14th May 2007

Act of 21 May 1836 on the prohibition of lotteries

n°84-1208 of the December 29, 1984

Act of June 2, 1891

Act of May 13, 1996

Draft bill on online gambling ("Projet de loi relative à la concurrence et à la régulation du secteur des jeux d'argent et de hasard en ligne") in French

ARJEL

Book of specifications (cahier des charges) in French

Technical requirements (exigencies techniques) in French

FAQ (updated April 13, 2010)

12. Regulator and Operator Contacts

Ministère de l'Intérieur
Sous-Direction des Courses et des Jeux
11, rue des Saussaies
Paris, Ile-de-France 75800
France

Tel.33-1-49-27-49-27

ARJEL

Mission de préfiguration de l'ARJEL
99-101 rue Leblanc
75015 Paris
France
Email: questions@pre-arjel.fr

Operator Contact Details

Lottery and sports betting operator:

La Francaise des Jeux
126 Rye Galliéni
Boulogne Billancourt, Ile- de- France 92643
France
Tel. 33-1-41-10-35-35

Horse race betting operator:

Pari Mutuel Urbain
Direction Générale
2, rue du Professeur Florian Delbarre -
Paris, Ile- de- France 75734
France
Tel. 33-1-56-09-91-00

Casinos:

<u>Aix- les- Bains Grand Cercle Casino</u> 200 Rue du Casino Aix Les Bains, Rhone- Alps 73100 France Tel.33-4-79-35-16-16	<u>Casino de Hauteville Lompnes</u> 380 Frederic du Marest St. Hauteville Lompnes, Rhone- Alps 0110 France 33-4-74-40-07-07	<u>Grand Casino de Beaulieu</u> 4, avenue Fernand Dunan Beaulieu- sur- Mer, Province- Alpes- Cote d'Azur 06310 France 33-4-93-76-48-00
<u>Aviation Club de France</u> 104 Avenue des Champs- Elysees Paris, Ile- de- France 75008 France 33-1-45-62-26-88	<u>Casino de Megeve</u> 199, rue Charles Feige Megeve, Rhone- Alps 74120 France 33-4-50-93-01-83	<u>Group Cogit Casinos</u> Rue des Alizes BP 7133 Schoelcher, Martinique 97277 France 33-5-96-61-99-06
<u>Bourbonne- les- Bains Casino</u> 1 Place des Bains Bourbonne- les- Bains, Champagne- Ardenne 52400 France 33-3-25-90-90-90	<u>Casino de Palavas- les- Flots</u> 1 Boulevard Foch Palavas- les- Flots, Languedoc- Roussillon 34250 France 33-4-67-68-00-01	<u>Groupe Emeraude</u> 112 Bis Boulecard Malesherbes Paris 75017 France 33-1-56-79-09-10
<u>Casino de Brides</u> Esplanade des Thermes Brides les Bains, Rhone- Alps 73570 France 33-4-79-55-23-07	<u>Casino de Quiberon</u> 2, Boulevard Rene Cassin Quiberon, Bretagne 56170 France 33-2-97-50-23-57	<u>Cujan Mestras Casino</u> Lake Magdeleine Gujan Mestras 33470 France 33-5-57-73-00-78
<u>Casino d'Ajaccio</u> Boulevard Pascal Rossini Ajaccio, Corse 20000 France 33-4-95-50-40-60	<u>Casino de Vals les Bains</u> Avenue Claude Expilly Vals les Bains, Rhone- Alps 07600 France 33-4-75-88-77-77	<u>Joa Groupe</u> Cite Internationale 34 quai Charles de Gaulle 06 Lyon Cedex 69463 33-4-72-56-22-30
<u>Casino de Cauteret</u> Esplanade des Oeufs Cauterets, Midi- Pyrenees 65110 France 33-5-62-92-52-14	<u>Casino des Dunes</u> Avenue de la Plage La Faute sur Mer 85460 France 33-2-51-27-10-29	<u>L'Imperial Palace</u> Allee de l'Imperial Parc de l'Imperial Annecy, Rhone- Alps 74000 France 33-4-50-09-30-00
<u>Casino de Cayeux</u> 800, boulevard du General Sizaire Cayeux sur Mer, Picardie 80410 France	<u>Casino d'Evian</u> Quai Baron de Blonay Evian les Bains, Rhone- Alps	<u>Le New Castel Casino Challes- les- Eaux</u> 229, avenue Comenget

France 33-3-22-26-71-56 <u>Casino de Chatel- Guyon</u> Place Brosson Chatelguyon, Auvergne 63140 France 33-4-73-86-00-39 target="_blank">Casino de Chaudes- Aigues 29 Place du Gravier Chaudes- Aigues, Auvergne 15110 France 33-4-71-23-54-67 <u>Casino de Dieppe</u> 3 Boulevard de Verdum Dieppe, Haute- Normandie 76200 France 33-2-32-14-48-00 <u>Casino de Divonnes les Bains</u> Avenue des Thermes Divonne- les- Bains, Rhone- Alps 01220 France 33-2-50-40-34-34 Casino de Font Romeu 46 Avenue Emmanuel Brousse Font- Romeu, Languedoc- Roussillon 66120 France 33-4-68-30-01-11 <u>Casino de Granville</u> Place Marechal Foch Granville, Basse- Normandie 50400 France 33-2-33-50-00-79 <u>Casino de Grasse</u> Boulevard du Jeu de Ballon Grasse, Province- Alpes- Cote d'Azur 06130 France 33-4-93-36-91-00	74500 France 33-4-50-26-87-87 Casino Grand Cafe de Vichy 7 rue du Casino Vichy, Auvergne 03200 France 33-4-70-97-07-40 <u>Casino Le Lyon</u> 200 avenue du Casino La Tour de Salvagny, Rhone- Alps 69890 France 33-4-78-87-02-70 <u>Casino le Phoebus</u> Boulevard de la Sagne Gruissan, Languedoc- Roussillon 11430 France 33-4-68-49-02-52 <u>Casinos Groupe Tranchant</u> 84 AV du President Wilson Saint- Denis La Plaine Cedex 93214 France 33-1-48-20-35 <u>Casino Municipal D'Amneville</u> Parc de Coulange Amneville, Lorraine 57360 France 33-3-87-71-50-00 <u>Cercle Clichy Montmatre</u> 84, Rue de Clichy Paris, Ile- de- France 75009 France 33-1-48-78-32-85 <u>Cercle Wagram</u> 47 Avenue de Wagram Paris, Ile- de- France 75017 France 33-1-43-80-65-13	Cales- les- Eaux 73190 France 33-4-79-72-86-14 <u>Lucien Barrier Hotels and Casinos</u> 35 Boulevard des Capucines Paris 75002 France 33-5-59-22-77-77 <u>Noiretable Casino</u> Rue des Tilleuls Noiretable 42440 France 33-4-77-24-79-29 <u>Palm Beach</u> Place Franklin Roosevelt Cannes, Province- Alpes- Cote d'Azur 06400 France 33-4-97-06-36-90 <u>Partouche Casinos</u> 2, Avenue de l'Europe Annemasse, Rhone- Alps 74100 France 33-4-50-87-07-87 <u>Sofitel Royal Casino</u> 605, Avenue du General de Gaulle Mandelieu la Napoule, Province- Alpes- Cote d'Azur 06210 France 33-2-92-97-70-00 <u>Sporting Casino Hossegor</u> 119, avenue Maurice Martin Hossegor, Aquitaine 40150 France 33-5-58-41-99-99 <u>Vikings Casino</u> La Tuilerie Barbazan 31510 France 33-5-62-00-70-60
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¹ C-42/07, Liga Portuguesa de Futebol Profissional, Bwin International Ltd v Departamento de Jogos da Santa Casa da Misericórdia de Lisboa, September 8, 2009

² Article 2 of the law: "Est un jeu de hasard un jeu payant ou le hasard predomine sur l'habilete et les combinaisons de l'intelligence pour l'obtention du gain"

³ Article 3 (III)

⁴ Article 69

⁵ Art. 27: "Les sociétés de courses autorisées à organiser le pari mutuel hors les hippodromes, dans les conditions fixées par l'article 5 de la loi du 2 juin 1891 susvisée, en confient la gestion, pour leur compte, à un groupement d'intérêt économique qu'elles constituent entre elles dans les conditions fixées par l'ordonnance du 23 septembre 1967 susvisée. Les statuts de cet organisme, dénommé Pari mutuel urbain (PMU), sont approuvés par le ministre chargé de l'agriculture et le ministre chargé du budget. Lorsque le Pari mutuel urbain autorise des personnes privées à exploiter des postes d'enregistrement des paris, cette autorisation doit intervenir après enquête et avis favorable du ministre de l'intérieur."

⁶ Case C-212/08, OJ C 197 of 02.02.2008, p.12